No. 118585

IN THE
SUPREME COURT OF ILLINOIS

IN RE: PENSION REFORM LITIGATION	)	Appeal from the Circuit Court for the Seventh Judicial Circuit, Sangamon County, Illinois, Sangamon County Case Nos. 2014 MR 1, 2014 CH 3, and 2014 CH 48; Cook County Case No. 2013 CH 28406; and Champaign County Case No. 2014 MR 207 (consolidated pursuant to Supreme Court Rule 384) The Honorable JOHN W. BELZ, Judge Presiding

(Full caption on following pages)

BRIEF FOR DEFENDANTS-APPELLANTS

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No. 118585

IN THE
SUPREME COURT OF ILLINOIS

IN RE: PENSION REFORM LITIGATION	)	No. 2014 MR 1 Honorable JOHN W. BELZ
DORIS HEATON, PAMELA KELLER, KENNETH LEE, HATTIE DOYLE, JOHN SAWYER III, LANCE LANDECK, KYLE THOMPSON, and MICHAEL SCHIFFMAN, on behalf of themselves and a class of similarly situated persons, Plaintiffs-Appellees, v. PAT QUINN, in his capacity as Governor of the State of Illinois, JUDY BAAR TOPINKA, in her capacity as Comptroller of the State of Illinois, and THE BOARD OF TRUSTEES OF THE TEACHERS' RETIREMENT SYSTEM OF THE STATE OF ILLINOIS, Defendants-Appellants.	)	Originally Filed as Cook County Case No. 2013 CH 28406
RETIRED STATE EMPLOYEES ASS'N RETIREES, Lawrence Wort, Gladys Hajek, Linda Gueldener, and Mureen Richter, for themselves and on behalf of a class of persons similarly situated, Plaintiffs-Appellees, v. PATRICK QUINN, in his capacity as Governor of the State of Illinois, JUDY BAAR TOPINKA, Comptroller of the State of Illinois, DAN RUTHERFORD, Treasurer of State of Illinois, and THE BOARD OF TRUSTEES OF THE STATE EMPLOYEES RETIREMENT SYSTEM, Defendants-Appellants.	)	Originally Filed as Sangamon County Case No. 2014 MR 1

ILLINOIS STATE EMPLOYEES ASS'N RETIREES, ROBERT SILGER, GWENN KLINGLER, BARBARA SCHOB, BARBARA MAXEINER, and JOHN MUNDSTOCK, on behalf of a Class of Persons Similarly Situated, Plaintiffs-Appellees, v. THE BOARD OF TRUSTEES OF THE STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS, THE BOARD OF TRUSTEES OF THE GENERAL ASSEMBLY RETIREMENT SYSTEM, THE BOARD OF TRUSTEES OF THE STATE TEACHERS' RETIREMENT SYSTEM, THE BOARD OF TRUSTEES OF THE STATE UNIVERSITY RETIREMENT SYSTEM, JUDY BAAR TOPINKA, Comptroller of the State of Illinois, and DAN RUTHERFORD, the Treasurer of the State of Illinois, Defendants-Appellants.	)	Originally Filed as Sangamon County Case No. 2014 CH 3
GWENDOLYN A. HARRISON, GARY F. KROESCHEL, CHRISTINE M. BONDI, JULIE A. YOUNG, STEPHEN C. MITTONS, MONICA S. BUTTS, GARY L. CIACCIO, THOMAS W. TATE, JOSE M. PRADO, EDWARD F. CORRIGAN, CARYL E. WADLEY-FOY, ELLEN M. LARRIMORE, LEE A. AYERS, JAMES S. SHERIDAN, J. TODD LOUDEN, KENNETH N. DUGAN, JENNIFER L. EDWARDS, D'ANN URISH, JAMES P. HERRINGTON, TERRI L. GIFFORD, MICHAEL E. DAY, DENISE M. FUNFSINN, ELAINE G. FERGUSON, MARLENE M. KOERNER and DAVID L. BEHYMER, for themselves and on behalf of a class of all persons similarly situated, and WE ARE ONE ILLINOIS COALITION, Plaintiffs-Appellees, v. PATRICK QUINN, not individually but solely in his capacity as Governor of the State of Illinois, JUDY BAAR TOPINKA, not individually but solely in her capacity as Comptroller of the State of Illinois,	)	Originally Filed as Sangamon County Case No. 2014 CH 3

DAN RUTHERFORD, not individually but solely in his capacity as Treasurer of the State of Illinois, TEACHERS' RETIREMENT SYSTEM OF THE STATE OF ILLINOIS, BOARD OF TRUSTEES OF THE TEACHERS' RETIREMENT SYSTEM OF THE STATE OF ILLINOIS, STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS, BOARD OF TRUSTEES OF THE STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS, STATE UNIVERSITIES RETIREMENT SYSTEM OF ILLINOIS, and BOARD OF TRUSTEES OF THE STATE UNIVERSITIES RETIREMENT SYSTEM OF ILLINOIS, Defendants-Appellants.	)	
ILLINOIS STATE EMPLOYEES ASS'N RETIREES, ROBERT SILGER, GWENN KLINGLER, BARBARA SCHOB, BARBARA MAXEINER, and JOHN MUNDSTOCK, on behalf of a Class of Persons Similarly Situated, Plaintiffs-Appellees, v. THE BOARD OF TRUSTEES OF THE STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS, THE BOARD OF TRUSTEES OF THE GENERAL ASSEMBLY RETIREMENT SYSTEM, THE BOARD OF TRUSTEES OF THE STATE TEACHERS' RETIREMENT SYSTEM, THE BOARD OF TRUSTEES OF THE STATE UNIVERSITY RETIREMENT SYSTEM, JUDY BAAR TOPINKA, Comptroller of the State of Illinois, and DAN RUTHERFORD, the Treasurer of the State of Illinois, Defendants-Appellants.	)	Originally Filed as Sangamon County Case No. 2014 CH 3
STATE UNIVERSITIES ANNUITANTS ASS'N, DOMINIC "NICK" AREND, JOYCE BEASLEY, BRUCE BUSBOOM, OLIVER CLARK, AIMEE DENSMORE, MARCIA HAMOR, MAUREEN MCCORD, RICHIE PANKAU, BRUCE REZNICK, AND YVONNE SERGENT, Plaintiffs-Appellees,	)	Originally Filed as Champaign County Case No. 2014 CH 3

v.

STATE UNIVERSITIES RETIREMENT SYSTEM, PATRICK QUINN, Governor of the State of Illinois, JUDY BAAR TOPINKA, Comptroller of the State of Illinois, DAN RUTHERFORD, Treasurer of the State of Illinois,

Defendants-Appellants.

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POINTS & AUTHORITIES

NATURE OF THE CASE

In a five-page order, the Circuit Court of Sangamon County, Illinois declared the General Assembly's response to the State's $100 billion unfunded pension-liability crisis unconstitutional in its entirety. The circuit court held that the Pension Clause of the Illinois Constitution must be read as absolute. As a result, it found there is no circumstance dire enough to justify any reduction in benefits contractually promised to the members of a public retirement system. The court thus determined that the Pension Clause uniquely strips the State of its police powers, which, under the substantially identical state and federal Contracts Clauses, have permitted the State for more than a century to adopt legislation altering contractual rights in limited, extraordinary circumstances. In response, Defendants in this consolidated litigation — various government officials and four state retirement systems — filed this direct appeal to this Court. This appeal is not from a jury verdict, and questions are raised on the pleadings.

ISSUES PRESENTED

1. The Pension Clause of the Illinois Constitution provides that membership in a public pension system is "an enforceable contractual relationship, the benefits of which shall not be diminished or impaired." Ill. Const. art. XIII, § 5 (A16). By establishing these enforceable contractual relationships, does the Pension Clause incorporate the long-accepted police-power limitation on contract rights, thereby allowing the State to modify pension contracts under limited circumstances?

2. The United States Supreme Court has long held that, as a matter of federal constitutional law, "a State is without power to enter into binding contracts not to exercise its police power in the future," because the police power is an essential attribute of sovereignty that the State must always maintain to provide for the welfare of its citizens. *U.S. Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 23 n.20 (1977) (citations omitted). Does this federal constitutional prohibition preclude a State from creating contract rights that are exempt from the State's police powers under any and all possible future circumstances, no matter how dire?

3. Even assuming *arguendo* that the circuit court correctly held that parts of Public Act 98–599 ("the Act") violate the Pension Clause, did the court err by failing to give effect to Section 97 of the Act, which provides that some provisions are severable from the rest of the Act, and instead by striking down the Act in its entirety?

JURISDICTIONAL STATEMENT

This Court has jurisdiction over this direct review action under Illinois Supreme Court Rule 302(a). The circuit court issued a written order on November 21, 2014 declaring Public Act 98–599 unconstitutional in its entirety. (A1-6). The circuit court supplemented that decision on November 25, 2014 by adding findings required by Illinois Supreme Court Rule 18. (A7). On November 26, 2014, Defendants filed a notice of direct appeal to this Court. (A19-20).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Pertinent constitutional and statutory provisions are set forth in the appendix to this brief at A16-18.

INTRODUCTION

The Pension Clause of the Illinois Constitution elevates the protection afforded to the pension benefits of members in state-funded retirement systems from revocable gratuities — the status of most such benefits before 1970 — to contractual rights. The scope of this protection thus tracks the constitutional protection provided to all other contractual rights. Accordingly, the contractual rights protected by the Pension Clause are subject to the State's authority to modify contracts under certain conditions, often referred to as the State's "police powers." Not only does the plain meaning of the Pension Clause compel this result, but it is explicit in the Clause's history and has been recognized by this Court.

The circuit court below, however, with virtually no discussion or analysis of the police-powers limitation, adopted Plaintiffs' unprecedented claim that the Pension Clause abrogates that limitation entirely. But if the Pension Clause really bars the State's exercise of its police powers under every possible circumstance, no matter how dire the consequences, then the "contractual relationship" the Clause creates is unlike any other contractual relationship ever recognized in American law. Black letter law has long established that "[a]ll contracts, whether made by the state itself, by municipal corporations or by individuals, are subject to . . . subsequent statutes enacted in the *bona fide* exercise of the police power." *Hite v. Cincinnati, Indpls. & W. R.R. Co.*, 284 Ill. 297, 299 (1918); *see also* Restatement (Second) on Contracts § 608 cmt. b (1981). Treating pension benefits as "super-contracts" — rights entirely beyond the reach of the State's police powers — is thus not consistent with the plain meaning of the Pension Clause. It is instead a major and unprecedented reformulation of the

meaning of a "contractual relationship."

By recognizing that the Pension Clause, like the federal and Illinois Contracts Clauses, preserves the State's police power, this Court will not be granting the State a license to modify its own contractual obligations whenever it merely prefers not to fulfill those obligations. The police-power authority permits such modifications only in very limited circumstances. Nor will this Court be determining at this time whether the particular modifications the Act makes to the pension system are permissible exercises of the State's police powers in light of the circumstances. That question must be considered, in the first instance, by the circuit court on remand and based upon a full evidentiary record. But by rejecting the lower court's unyielding super-contract holding, this Court will preserve the longstanding balance between individual contractual rights and the State's sovereign duty to provide for the general welfare that is at the heart of our constitutional structure.

STATEMENT OF FACTS

I. The Retirement Systems and the Great Recession.

In 2013, as a result of the Great Recession, the General Assembly faced a crisis in the State's finances.[1] State revenues had plummeted, state services had been slashed, and the state retirement systems' unfunded pension liabilities had ballooned to approximately $100 billion. (SB Ex. 2 at 11-22; SB Ex. 4 at 13-31; SB Ex. 5 at 2-7; *compare* SB Ex. 1 at 70 *with* SB Ex. 1 at 73). The pension

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[1] Cites to the Bates stamped portion of the record on appeal will be denoted by "C" followed by the relevant page numbers. "SB" refers to a binder of exhibits (including exhibits on an included disk) in the Appendix to Defendants' Statement of Facts in support of their Motion for Summary Judgment, referred to as a "Separate Binder" in the Index to the Record on Appeal. The pages of the binder were not individually Bates stamped by the circuit court.

shortfall negatively affected the State's overall finances and long-term financial health. (*E.g.*, SB Ex. 2 at 11-22; SB Ex. 4 at 13-31; SB Ex. 5 at 2-7.)

A. *The Great Recession and the causes of the crisis.*

The Illinois state-funded retirement plans at issue consist of the Teachers' Retirement System of the State of Illinois ("TRS"), the State Universities Retirement System of Illinois ("SURS"), the State Employees' Retirement System of Illinois ("SERS"), and the General Assembly Retirement System of Illinois ("GARS") (collectively, "the systems"). Pub. Act 98–599, § 15. Before 1994, the State had made annual contributions to the systems that were lower than necessary to put them in a fully funded condition,[2] a practice repeatedly upheld as constitutional. *See, e.g., People ex rel Ill. Fed'n of Teachers v. Lindberg*, 60 Ill. 2d 266, 272 (1975); *McNamee v. State of Ill.*, 173 Ill. 2d 433, 446 (1996). But in 1994, the General Assembly passed a law setting a new contribution schedule that would bring the systems to a 90% funding level by 2045. (SB Ex. 1 at 14.) As of 2006, the State was on track to pay down the systems' unfunded liabilities pursuant to that schedule. (SB Ex. 2 at 14-15.)

Then the Great Recession, an economic crisis of a size and duration not seen since the Great Depression of the 1930s, (SB Ex. 2 at 7, 9), derailed that plan and wreaked havoc with the State's finances. In the short term, the Great Recession resulted in a unprecedented 12% drop in base state revenues, (SB Ex. 5 at 2-3), marking the first time in decades (with the exception of a minor

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[2] A pension plan is fully funded when it has enough assets to pay promised benefits for past services based on actuarial assumptions about future investment earnings and member salaries, retirement dates and life expectancies. A plan is underfunded when it does not have sufficient assets to pay those benefits. (SB Ex. 1 at 4-5, 9-12, 19.)

reduction in 2002) that the State's annual revenues did not increase, (*id.*). In particular, income taxes, the State's largest revenue source, declined by almost 20% between 2008 and 2010. (SB Ex. 2 at 18.) In addition, the need for basic state-funded services spiked. For example, Medicaid eligibility increased by 28%, and Temporary Assistance for Needy Families increased by 78%. (SB Ex. 5 at 4; SB Ex. 4 at 23.) Thus, during the Great Recession, the State took in substantially less revenue while facing dramatically increased demands for some of its most basic services.

The Great Recession also had a substantial negative effect on the state-funded pension systems themselves. Between 2008 and 2010, the systems' assets lost more than 30% of their value, falling from $70 billion to $48 billion. (SB Ex. 4 at 5.) Moreover, as it did for many investors, the Great Recession forced the systems' actuaries to significantly lower their assumed rate of future returns on investments, further increasing the systems' underfunding. (SB Ex. 1 at 30.) As a result, the systems' unfunded pension liabilities increased from $41 billion in 2007 to almost $100 billion in 2012. (SB Ex. 1 at 72-73.) So although the systems were almost 75% funded in 2000, by 2010 their combined funding ratio had dropped to about half that amount, 38.5%, and four years later had risen only to 41%. (SB Ex. 1 at 60.) At 41%, Illinois' pension system is the worst-funded state system in the country. (SB Ex. 3 at 3.)

By the end of the Great Recession, the fundamentals of State's long-term budget had changed: While in 2007 the State's annual pension costs accounted for only about 5.6% of its General Revenue Fund ("GRF"), by 2014, pension costs had spiked to over 20% of GRF. (SB Ex. 2 at Ex. T; SB Ex 7.)

In addition, before the Great Recession, and even more so during it, the annual rate of inflation dropped. (SB Ex. 2 at 26.) In 1989, the General Assembly raised the guaranteed annual increases in pension benefits, sometimes referred to as COLAs, to 3% compounded annually to provide some protection for pensioners' purchasing power. (SB Ex. 2 at 3.) But at that time, inflation was above 4.5% and was expected to continue between 4% and 4.5%. (SB Ex. 2 at 26.) That expectation never came to pass. Instead, inflation first declined to about 3%, (*id.*), and then from year-end 2007 through year-end 2013, it plummeted: The Consumer Price Index ("CPI") averaged only 1.7% annually during that period, and it is predicted to remain below 2.5% in the future. (*Id.*) Since 1997 and going forward, the impact on the systems of providing pensioners greater purchasing-power protection than originally expected amounts to $36 billion — or more than a third of the systems' unfunded liabilities. (SB Ex. 1 at 44-45.)

Dramatically increased longevity over the past two decades has also contributed to the increase in the systems' unfunded liabilities. (SB Ex. 1 at 32-36.) As people live longer and actuaries change their assumptions accordingly, the systems need more money to be fully funded. (SB Ex. 1 at 34.) The pace at which longevity has increased came as a surprise to actuaries and experts and was not therefore captured in many of the actuarial predictions used for funding pensions. (SB Ex. 1 at 32-33.) In Illinois, the combination of past longevity improvements and future expected improvements has increased the systems' liabilities by a total of $9 billion. (SB Ex. 1 at 36.)

B. *The General Assembly's responses to the Great Recession.*

During the Great Recession, the General Assembly responded to these extreme financial pressures without making any changes to pension benefits for

existing members of the pension systems. It temporarily increased income taxes, (SB. Ex. 5 at 4), despite the negative economic impact of doing so at a time of unusually and stubbornly high unemployment and unusually low household incomes (SB Ex. 2 at 6-7, 10, 17 & Exs. A, I, P). It also cut spending by reducing or eliminating basic state services. For example, it cut Medicaid provider rates and eliminated or reduced funding for numerous education programs (SB Ex. 4 at 16, 18-19; SB Ex. 3 at 20-21); and it cut the operating budgets for the Division of Alcohol and Substance Abuse (18%), Division of Mental Health (29%), the Department of Public Health (grants reduced 73%), and the Department of Children and Family Services (6%), (SB Ex. 4 at 23-27). It deferred billions of dollars in payments owed to state vendors and creditors, resulting in a backlog of more than $7 billion in unpaid bills in 2013, (SB Ex. 5 at 7), on much of which the State must pay interest, 30 ILCS 540/3-2 (2012). And it enacted a separate program of less generous pension benefits for new employees. (SB Ex. 5 at 7.)

Yet even after all of these reforms, the share of general state revenues required for payments to the systems skyrocketed — from under 6% in 2007 to over 20% of general revenues by 2014. (SB Ex. 2 at Ex. T; SB Ex. 7; SB Ex. 12.) And the State's pension crisis caused a progressive deterioration in its credit rating, resulting in higher financing costs for its debt in the bond market and a corresponding loss of more than $1 billion in state funds. (SB Ex 6 at 5-8.)

In sum, at the end of 2013, in the face of increased demand for state services, the State already had increased taxes and drastically reduced spending by cutting programs for its most vulnerable citizens, *see supra*, yet it still faced unfunded pension liabilities of approximately $100 billion, consuming more than 20% of the State's GRF for the next generation, (SB. Ex. 3 at 7). The severity of

the crisis, and the need for legislative action, was recognized by plaintiff We Are One Illinois Coalition, which stated in a 2012 press release:

> The workers in Illinois want a real pension solution and we invite the state's political leaders to work with us in finding real solutions that can be enacted soon. There is no doubt that *a long-term pension solution is a long-term fiscal solution and that must involve truly shared sacrifice.*

(SB 27 (emphasis added).)

II. Public Act 98–599 and Its Effects

A. *The General Assembly's response*

Faced with these financial realities, the General Assembly concluded — in legislative findings in the Act itself — that "the fiscal problems facing the State and its retirement systems cannot be solved without making some changes to the structure of the retirement systems." Pub. Act 98–599, § 1 (A17). The legislature concluded that those changes would have to involve a mix of stricter funding requirements for the State, and reductions in future COLAs for members the systems. *Id.* These COLA reductions were structured to minimize the impact on those with the lowest pensions and longest periods of public service, as well as on those already retired or closest to retirement. C2118. No pensioners will experience reductions in their pensions. *Id.*

The Act does not require members to contribute to the portion of unfunded pension liability that is attributable to the General Assembly's pre-1994 practice of paying contributions lower than necessary for the systems to be fully funded. (SB Ex. 1 at 31, 47; SB Ex. 3 at 9.) Instead, the Act reduces future COLAs *only* to recover a portion of the liability attributable to the Great Recession — and in fact to recover less than half of that amount. The Great Recession caused

approximately $43 billion of the unfunded liability (SB Ex. 1 at 31); the Act's COLA reductions will eliminate about $20 billion of that amount, (SB Ex. 1 at 47.) The savings (calculated for accrued benefits alone) that the Act provides amount to $1.3 billion a year. (SB Ex. 3 at 9.)

First, the General Assembly committed to a funding schedule that achieves 100% funding by 2044. Pub. Act 98–599, § 15 (amending 40 ILCS 5/2-124, 14-131, 15-155, 16-158). The schedule mandates consistent annual payments on an actuarially sound basis and requires the State to contribute an additional $364 million in fiscal year 2019, $1 billion annually thereafter, and beginning in 2016, 10% of the annual savings resulting from the rest of the legislation until the system reaches 100% funding. Pub. At 98–599, § 10 (amending 30 ILCS 122-20). And unlike prior law, the Act creates a judicial enforcement mechanism to compel the State to make its required contributions should it fail to do so. Pub. Act 98–599, § 15 (amending 40 ILCS 5/2-125, 14-132, 15-156, and adding 40 ILCS 5/16-158.2).

Second, as already noted, the General Assembly reduced future COLAs from the 1989 rate of 3% compounded annually. *Id.* (amending 40 ILCS 5/2-119.1, 14-114, 15-136, 16-133.1). Because inflation dropped so significantly after 1989, the guaranteed COLA of 3% compounded annually had long outpaced the purchasing-power protection it was expected to provide. (SB Ex. 2 at 26.) The General Assembly apportioned the reductions in COLAs to minimize the impact on those who could least afford them; members with low salaries would see little or no change; and members with the most years of public service would experience the smallest reductions. Current retirees would experience smaller reductions than current employees, and current employees with the most

accumulated service would see smaller reductions than more recently hired workers. Finally, current employees' required contributions to the pension systems were reduced. Pub. Act 98–599, § 15 (amending 40 ILCS 5/2-124, 14-131, 15-155, 16-158).

B. *Effects on Illinois in the absence of the Act.*

Without the savings of the Act, pension costs as a share of tax revenues will continue to increase for at least the next fifteen years, peaking at between 20% and 25%. (SB Ex. 3 at 7.) That means at least one of every five dollars — and possibly as much as one of every four dollars — of tax revenue collected by the State will have to go to pension costs. (*Id.*) Pension costs, which in 2013 were $5.7 billion, will rise with or without the Act, but without the Act the State will have to raise taxes and/or cut spending enough to replace the $1.3 billion savings (from accrued benefits alone) that the Act saves annually. (SB Ex. 3 at 2, 7, 9-10.) These taxes or spending cuts would be in addition to the measures taken by the State to cover the rest of the increased pension contributions caused by the Great Recession. (SB Ex. 1 at 68.)

Illinois has the nation's 15th highest state and local tax burden, and has a higher tax burden than any Great Lakes State other than Wisconsin. (SB Ex. 3 at 11.) If Illinois had to raise an additional $1.3 billion a year in taxes, annual per capita state taxes would increase 3.4% (SB Ex. 3 at 10), and these increases would add disproportionately to the tax burdens of lower income households, (SB Ex. 3 at 14). Because this additional revenue would fund pension contributions, Illinois residents would receive no additional public services as a result of those tax increases. (*Id.*)

This additional tax burden would, over time, have a negative impact on the State's economic growth of approximately 1.1%. (SB Ex. 3 at 16.) The long-run impact of the tax increase would be a loss of between approximately 38,000 and 64,000 jobs. (*Id.*) It would be especially challenging for Illinois to retain manufacturing and transportation businesses, which hire semi-skilled workers at decent wages. (SB Ex. 2 at 22.) Increased taxes can also lead individuals and businesses to relocate to other States, thus further eroding Illinois' tax base. (SB Ex. 2 at 24.)

Although Illinois has a relatively high tax burden, the State, which cut spending during the Great Recession, has per-capita state spending (measured as a share of personal income) that is the 10th lowest of the 50 States. (SB Ex. 3 at 17.) Much of the State's spending is mandatory and so cannot be cut. (SB Ex. 4 at 1-2; SB Ex. 5 at 1-2, 8.) That means cuts in spending would have to come primarily from education, health care, and public safety, which are areas that have already experienced significant cuts in recent years. (SB Ex. 5 at 7-11.)

And the State faces other significant needs. For example, the American Society of Civil Engineers' 2014 infrastructure report card gives the State a C-grade, and singles out roads, transit, and water infrastructure as being of particularly poor quality. (SB Ex. 3 at 23.) The same report estimated that $30.9 billion is needed to bring Chicago's regional transit to a state of good repair and $17.5 billion is needed to replace and upgrade wastewater systems throughout the State. (*Id.*) The 2012 State Budget Crisis Task Force reported that Illinois' infrastructure would require $340 billion over the next 30 years to maintain, upgrade, expand, and replace public capital assets, with roads and bridges accounting for a large share of that total. (*Id.*)

III. Proceedings Below

Plaintiffs are members of the four systems, a coalition of labor unions, and three public employee advocacy organizations. C3-4, 199-201, 247-48, 314. In five different complaints filed in three different Illinois counties — which were consolidated by this Court into a single, consolidated action in the Circuit Court of Sangamon County, C686 — they all challenged the constitutionality of the Act's provisions curbing the size of their future COLAs and, in some instances, other less significant modifications, C3, 199, 247, 314. In their answers, Defendants alleged that under the particular factual circumstances surrounding the Act's passage, the Act constituted a legitimate exercise of the State's police powers. *E.g.* C1353-59 (A9-15). Plaintiffs filed a joint reply denying these allegations. C1494-1508.

Plaintiffs later filed three separate motions: a motion for summary judgment, C1927, a motion for judgment on the pleadings, C2019, and a motion to strike the affirmative matter from Defendants' answers, C2006. In each of those motions, Plaintiffs claimed that the Pension Clause eliminates entirely the State's police powers and thus does not permit modification of the contractual benefits of membership in the systems under any circumstances. C1927, 2006, 2019. Defendants, in turn, filed a cross-motion for summary judgment, arguing that there was no genuine issue of material fact as to the validity of the Act, given the causes and extent of the State's severely strained financial condition and related unfunded pension liabilities. C2134.

The circuit court ordered Defendants to respond to Plaintiffs' motions, but did not similarly require Plaintiffs to respond to Defendants' motion. C2065. Following briefing on Plaintiffs' motions, the court ordered both parties to submit

proposed orders to the court. *See* C2318-20. One day after oral argument, the court signed Plaintiffs' five-page draft as its opinion with only minor, stylistic alterations, *compare* C2321-25, *with* C2312-17 (A1-6), holding that "as a matter of law[,] the [D]efendants' [police-powers defense] provides no legally valid defense," C2315 (A4). The opinion concluded that the language of the Pension Clause is "absolute and without exception." C2314-15 (A3-4).

The opinion contained no further analysis about the text, meaning, or purpose of the Pension Clause. Nor did it address most of Defendants' arguments, including their contentions that (1) the "contractual relationship" protected by the Pension Clause should be read as coextensive with the protection traditionally afforded to contractual rights by the Contracts Clauses of the state and federal Constitutions, and (2) that the federal Constitution prohibits the State from divesting itself of its police powers. Finally, the circuit court struck down the entire Act, despite statutory language identifying a limited number of provisions as inseverable, thus leaving the remainder severable. C2315-16 (A4-5).

ARGUMENT

The constitutional protections of the Pension Clause are the same as those afforded to all contractual relationships, which even under the Illinois and federal Contracts Clauses are not absolute, and are thus subject to various limitations. The circuit court, however, ignored those limitations, including the State's long-recognized ability to modify contracts in extraordinary circumstances pursuant to its police powers. The circuit court's holding thus creates an unprecedented and unworkable rule of law: under no circumstance, no matter what emergency or unforeseen event arises, can the State reduce pension benefits by so much as a penny.

That holding flouts the Clause's plain meaning. The Pension Clause grants members in a public retirement system a *contractual* right to benefits, not an entitlement immune from the standard limitations applicable to all contracts. And courts have recognized, since even before the Civil War, that one of the most important of these limitations is the legitimate exercise of the State's police powers. The circuit court ignored this longstanding and uncontroversial understanding of the Clause's plain meaning and converted public pensions into unprecedented super-contracts.

Any arguable ambiguity as to this plain meaning is settled by the historical record. When the drafters of the Illinois Constitution defined the protection of the Pension Clause as a *contractual* protection, they made no mention, either in the text of the Clause or in the debates surrounding its adoption, of any desire to deviate from the longstanding police-powers doctrine. In fact, the drafters of the Illinois Constitution had an altogether different aim: upgrading public pension benefits from gratuities to contractual rights. That is crucial because in 1970,

almost all public pension benefits were non-contractual and thus subject to the whim of the legislature. By affording all public pension benefits the *same* protection afforded to all contracts with the government, the drafters were responding to the state of the law at the time. But never once did they suggest that the Pension Clause created *greater* protection than the protection traditionally afforded to contractual relationships.

Nor is the circuit court's holding consistent with precedent construing the Pension Clause itself. In fact, the decision below is the first time any court has held that the Pension Clause creates rights in excess of traditional contractual guarantees. Surely if the rights created by the Pension Clause were so fundamentally different from every other contractual right previously recognized in American history, at some point during the Constitutional Convention or in the forty-five years since the Clause's adoption there would have been some explicit declaration acknowledging that departure. The opposite is true, however. When this Court considered whether police-power standards apply to benefits protected by the Pension Clause, it did not reject the defense on its face (as the circuit court did here), but evaluated the defense on its *factual* merits. *Felt v. Bd. of Trustees of Judges Ret. Sys.*, 107 Ill.2d 158, 166 (1985).

Moreover, the circuit court's extreme view of the Pension Clause so undermines the State's sovereignty that it violates basic federal constitutional principles. The federal Constitution requires the States always to reserve enough authority to respond to extraordinary threats to the public welfare. Yet despite this bedrock tenet of federal constitutional law, the court construed the Pension Clause as an absolute guarantee that sweeps away the State's police powers.

In the end, the circuit court's absolutist and unprecedented view of the Pension Clause runs afoul of the plain meaning of the pertinent constitutional language, the clear objectives of the drafters of the 1970 Constitution, this Court's precedent, and a fundamental federal constitutional doctrine. Its embrace of that radical and unqualified reading must be reversed.

I. Standard of Review

The circuit court held that Public Act 98–599 was unconstitutional against the backdrop of three different motions brought under three different sections of the Code of Civil Procedure, all arguing that Defendants' reliance on the State's police powers was completely foreclosed as a matter of law. C2316 (A5); *see* C1927, 2006, 2019. The circuit court's resolution of each of those motions is reviewed *de novo*, in part because "[t]he constitutionality of a statute is a question of law that is reviewed *de novo*." *Cwik v. Giannoulias*, 237 Ill. 2d 409, 416 (2010).

"All statutes carry a strong presumption of constitutionality." *In re Marriage of Miller*, 227 Ill. 2d 185, 195 (2007). "The presumption of validity means that courts must uphold a statute's constitutionality whenever reasonably possible." *Beaubien v. Ryan*, 198 Ill. 2d 294, 298 (2001). Thus, "[c]ourts have a duty to . . . resolve all doubts in favor of constitutional validity." *People ex rel. Sheppard v. Money*, 124 Ill. 2d 265, 272 (1988). "The burden of rebutting this presumption is on the party challenging the validity of the statute." *Hope Clinic for Women, Ltd. v. Flores*, 2013 IL 112673, ¶ 33. To carry this burden, the party challenging a law's validity must "demonstrat[e] a clear constitutional violation." *In re Derrico G.*, 2014 IL 114463, ¶ 54.

II. The Pension Clause Does Not Eliminate the State's Inherent Police-Power Authority to Modify Contractual Obligations When Doing So Is Necessary to Protect the General Public Welfare.

A. The Plain Meaning of the Pension Clause Recognizes Standard Contractual Rights Which Are Subject to the Legitimate Application of the State's Police Powers.

The Pension Clause, which was added to the Illinois Constitution of 1970, provides, in relevant part:

> Membership in any pension or retirement system of the State . . . shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.

Ill. Const. art XIII, § 5 (A16). The plain meaning of this Clause allows the State to exercise its police powers under certain extraordinary circumstances to modify pension contracts.

The Clause creates a "contractual relationship." Yet the circuit court entirely failed to evaluate or discuss the recognized attributes of a contractual relationship, even as it claimed — in an opinion drafted by Plaintiffs — that the text is "plain" and "unambiguous." C2312 (A1). But the plain and unambiguous meaning of a "contractual relationship" incorporates the black-letter rule that "[a]ll contracts . . . are subject to . . . subsequent statutes enacted in the *bona fide* exercise of the police power." *Hite*, 284 Ill. at 299.

This rule is not controversial. Even the Second Restatement on Contracts declares that a contract that was valid at its inception may later be modified or invalidated by "the police power of the State." Restatement (Second) on Contracts § 608 cmt. b (1981); *see East N.Y. Sav. Bank v. Hahn*, 326 U.S. 230, 232 (1945) (explaining that application of State's police powers "may be treated as an implied condition of every contract and, as such, as much part of the contract as

though it were written into it"); *see also Hudson County Water Co. v. McCarter*, 209 U.S. 349, 357 (1908) (Holmes, J.) ("One whose rights, such as they are, are subject to state restriction, cannot remove them from the power of the State by making a contract about them."). Moreover, the Pension Clause's language parallels the Contracts Clauses' protections against contract impairment by using the phrase "diminished or impaired," thus establishing a protection that mirrors those Clauses' recognition of the State's police powers.

Despite the clarity of this plain meaning, by the circuit court's unprecedented and unbounded logic, the Illinois Constitution permanently and irrevocably ties the hands of future generations, even if they face the most dire of circumstances. According to the circuit court's holding, for example, faced with an epidemic requiring the State to purchase and distribute vaccines or other costly medication, the State could not even temporarily reduce pension benefits to cover those costs. Likewise, if the State's bond rating collapsed, making borrowing impossible, the State could not modify pensions even if, as a consequence, it had to close its prisons and schools. Nor, in a period of prolonged deflation, similar to Japan in the 1990s, could the State reduce pension benefits, even if the corresponding rise in benefits caused by 3% annually compounded COLAs caused every dollar of state revenue to be spent on pension benefits. These consequences are all the more grave in light of the fact that, unlike private parties and municipal governments, the State cannot declare bankruptcy.

While those precise circumstances may not be presented here, they are the necessary extension of the circuit court's extreme holding. That radical result simply cannot be squared with the plain meaning of a "contractual relationship," which has long recognized the exercise of a state's police powers as a limitation

on the constitutional protection afforded to contractual rights. The Pension Clause did not *sub silentio* undo this long established plain meaning, and it does not create super-contracts for public pension benefits. To the contrary, the Clause establishes that public pension benefits are contractual rights and thus subject to the same limitations as all other contractual rights. Accordingly, the circuit court's disregard of the Clause's plain meaning cannot withstand scrutiny.

1. The Circuit Court Erred When It Ignored a Century and a Half of Federal and State Law Defining All Contractual Relationships As Inherently Subject to the State's Police Powers.

Both the Illinois and the United States Constitution prohibit any law "impairing the obligation of contracts." U.S. Const. art. I, § 10; Ill. Const. art. I, § 16. Despite this language, which contains no explicit qualifications, both this Court and the United States Supreme Court have long held that this prohibition "must be accommodated to the inherent police power of the State 'to safeguard the vital interests of its people.'" *Energy Reserves Grp. v. Kan. Power & Light Co.*, 459 U.S. 400, 410 (1983) (quoting *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 434 (1934)); *see George D. Hardin, Inc. v. Vill. of Mt. Prospect,* 99 Ill. 2d 96, 103 (1983); *see also W.B. Worthen Co. v. Thomas*, 292 U.S. 426, 433 (1934) ("[L]iteralism in the construction of the Contract Clause . . . would make it destructive of the public interest by depriving the State of its prerogative of self-protection."). Thus, the circuit court's conclusion that contractual rights to public pensions are absolute right is contrary to more than 150 years of American law.

Illinois has had a Contracts Clause in its Constitution since 1818, *see* Constitution of 1818, art. VIII, § 16; Constitution of 1848, art. XIII, § 17;

Constitution of 1870, art. II, § 14, and that provision has never explicitly mentioned the police power. Nevertheless, this Court has consistently recognized that authority, including in connection with the State's own contracts. *See, e.g.*, *Hite*, 284 Ill. at 299; *see also* George D. Braden & Rubin G. Cohn, *The Illinois Constitution: An Annotated and Comparative Analysis* 71-72 (1969) (discussing history of "the ever present, formidable police power concept" that "has permitted the exercise of legislative power which clearly interfered with, abridged or in some cases abolished contract rights"). By 1845, this Court already had resolved that contractual rights conferred by the government are not absolute, but instead are "subject to an implied reservation in favor of the sovereign power." *Mills v. St. Clair Cnty.*, 7 Ill. 197, 227 (1845). In 1869, it upheld a law authorizing the City of Chicago to grant licenses to sell alcohol within one mile of the University of Chicago, even though the University's state-issued charter barred such sales, because the new law "emanat[es] from the police power of the State," which is not "subject [to] irrevocable grant." *Dingman v. People*, 51 Ill. 277, 280 (1869). And in 1878, the Court held that a state-issued railroad charter expressly allowing the railroad to set its own rates could not prevent the State from setting a maximum rate to protect the public from monopoly pricing. *Ruggles v. People*, 91 Ill. 256 (1878).

By the turn of the century, this Court had become even more emphatic: "No contract can be made which assumes to surrender or alienate a strictly governmental power which is required to continue in existence for the welfare of the public. This is especially true of the police power, for *it is incapable of alienation.*" *City of Chi. v. Chi. Union Traction Co.*, 199 Ill. 259, 270 (1902) (internal quotation omitted) (emphasis added). Thus, the Court upheld a law

limiting recovery on publicly issued bonds because it "was intended to meet a distressed financial condition prevalent throughout the State." *Town of Cheney's Grove v. VanScoyoc*, 357 Ill. 52, 55, 61-62 (1934). And in *City of Chi. v. Chi. & Nw. Ry. Co.*, this Court upheld a statute altering the contractual allocation of construction costs on public property, holding that a contractual right does "not prevent a proper exercise by the State of its police power of enacting regulations reasonably necessary to secure the health, safety, morals, or general welfare of the community, even though contracts may thereby be affected, for such matters cannot be placed by contract beyond the power of the State to regulate and control them." 4 Ill. 2d 307, 317-18 (1954).

This rule does not mean that agreements between the State and private parties are illusory or may be modified at the State's whim. Under ordinary circumstances States will be held to their contractual commitments. Indeed, in many cases recognizing the police-powers defense, the courts nonetheless conclude that the use of the police powers was not warranted.[3] *E.g.*, *Felt*, 107 Ill. 2d at 167. Yet there are important reasons for the police-powers limitation. As already discussed, a State that lacks the ability to modify contracts under

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[3] Defendants' affirmative motion for summary judgment explained that the Act will be upheld only if it is "'reasonable and necessary to serve an important public purpose.'" C2155 (quoting *U.S. Trust Co.*, 431 U.S. at 25). Courts applying that test have considered a variety of factors, including the degree of the impairment and how it compares with legislative alternatives not adopted, *see, e.g.*, *Buffalo Teachers Fed'n v. Tobe*, 464 F.3d 362, 371 (2d Cir. 2006), the degree to which the events prompting the law were "unforeseen and unintended," *see, e.g.*, *Balt. Teachers Union v. Mayor & City of Council of Balt.*, 6 F.3d 1012, 1017-18 (4th Cir. 1993), and the degree to which the contractual modifications of the challenged law specifically targets the problems prompting its passage, *Md. State Teachers Ass'n v. Hughes*, 594 F.Supp. 1353, 1366-70 (D. Md. 1984); *Felt*, 107 Ill.2d at 166.

appropriate circumstances might find itself unable to protect its citizenry from disease, the consequences of natural disaster, or economic collapse.[4] Indeed, the State's duty to protect its citizens in extraordinary situations is of federal constitutional dimension, *see infra,* Part III.

Nor is this Court unique in its treatment of the police powers. Its uninterrupted recognition that "[a]ll contracts, whether made by the state itself, by municipal corporations or by individuals, are subject to be interfered with or otherwise affected by subsequent statutes enacted in the *bona fide* exercise of the police power," *Hite*, 284 Ill. at 299, parallels the decisions of the United States Supreme Court. As in Illinois, even before the Civil War, the Supreme Court had made clear that the facially absolute language of the Contract Clause cannot be so interpreted. *West River Bridge Co. v. Dix*, 47 U.S. 507, 530-33 (1848); *see also Ogden v. Saunders*, 25 U.S. 213, 286 (1827) ("To assign to contracts, universally, a literal purport, and to exact for them a rigid literal fulfillment, could not have been the intent of the constitution.").

Accordingly, by the 1880s the Court had firmly established that no contract could foreclose a State's ability to exercise its police powers. *See Boston Beer Co. v. Massachusetts*, 97 U.S. 25, 32-33 (1877); *Boyd v. Alabama*, 94 U.S. 645, 650 (1876) ("We are not prepared to admit that it is competent for one legislature, by any contract with an individual, to restrain the power of a subsequent legislature

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[4] In addition, if a State could grant super-contracts, all manner of special interests would seek them, some successfully, and thus permanently exempt themselves from the State's governance, regardless of the general welfare. So odious is that prospect that the Illinois Constitution has long included another constitutional provision that bars the General Assembly from granting any type of super-contract. Ill. Const. art. I, § 16 (prohibiting any law "making an irrevocable grant of special privileges or immunities").

to legislate for the public welfare . . ."). Most prominently, in *Stone v. Mississippi*, the United States Supreme Court upheld a state constitutional provision prohibiting lotteries, even though just a year earlier the State, in consideration of $5,000, granted a company a 25-year charter to operate a lottery. 101 U.S. 814, 820 (1880). The Court explained:

> Irrevocable grants of property and franchises may be made if they do not impair the supreme authority to make laws for the right government of the State; *but no legislature can curtail the power of its successors to make such laws as they may deem proper in matters of police.*

Id. at 817-18 (emphasis added) (citation and internal quotation marks omitted).

As in Illinois, this line of cases continued into the 20th century, including in factual circumstances reminiscent of those at issue here. *Home Building and Loan Association*, for example, involved a State's response to the dire economic events of the Great Depression. 290 U.S. at 433-34. There, the United States Supreme Court upheld a Minnesota statute imposing a moratorium on mortgage foreclosures. Declaring it "beyond question that the prohibition [in the Contracts Clause] is not an absolute one and is not to be read with literal exactness like a mathematical formula," the Court emphasized that a State's duty to "safeguard the vital interests of its people" must be "read into contracts as a postulate of the legal order," which "presupposes the maintenance of a government . . . which retains adequate authority to secure the peace and good order of society." *Id.* at 428, 434-35.

In other words, like this Court, the United States Supreme Court has long recognized that, notwithstanding the facially absolute language of the Contracts Clause, extreme economic circumstances allow States to use their police powers

to modify contracts to protect the public welfare. *E.g.*, *Manigault v. Springs*, 199 U.S. 473, 479-80 (1905); *Faitoute Iron & Steel Company v. Asbury Park*, 316 U.S. 502, 506, 511 (1942) (upholding state legislation authorizing modification of public bonds and emphasizing that "[t]he necessity compelled by unexpected financial conditions to modify an original arrangement for discharging a city's debt is implied in every such obligation"); *see also Sanelli v. Glenview State Bank*, 108 Ill. 2d 1, 23-24 (1985).

This principle was beyond question when Illinois adopted the 1970 Constitution. Not only was there more than one hundred years of precedent, but only five years before the 1970 Constitution was adopted, the United States Supreme Court had upheld a law shortening the redemption period under government contracts for the sale of public land where the purchasers failed to make the annual payments. *City of El Paso v. Simmons*, 379 U.S. 497, 516 (1965). With the discovery of oil and gas below the lands, properties in default for many years were being redeemed, leading to "a costly and difficult burden on the State." *Id.* at 515. Upholding the challenged law, the Court relied on the State's police powers, "notwithstanding that they technically alter an obligation of a contract." *Id.*

Ignoring this longstanding precedent, the circuit court failed to apply the canon that "the drafters of a constitutional provision are presumed to know about existing laws and constitutional provisions and to have drafted their provisions accordingly." *Kanerva v. Weems*, 2014 IL 115811, ¶ 41. This was error. The Pension Clause's express language — establishment of a "contractual relationship" — reflects a decision to incorporate the same degree of protection afforded to all contracts, as this Court has recognized. *See Buddell v. Bd. of Trs.*,

State Univ. Ret. Sys. of Ill., 118 Ill. 2d 99, 102 (1987); *see also People ex rel Sklodowski v. State*, 162 Ill. 2d 117, 147 (1994) (Freeman, J., concurring in part and dissenting in part) ("The protection against impairment of state pension benefits is *co-extensive* with the protection afforded all contracts.") (emphasis added); *id.* at 148 (discussing test for legitimate exercise of police powers described in, *e.g,. U.S. Trust Co.*, 431 U.S. at 23-26, and *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 244-45 (1978), and noting there is no "material difference between the contract clause and the protection afforded under our own constitution" to pension benefits).

It is implausible that the lack of an explicit reference to the State's police powers in the Pension Clause means that those powers were silently eliminated. After all, the same could be said of the Contracts Clauses of the Illinois and United States Constitutions, both of which prohibit every law "impairing the obligation of contracts." U.S. Const. art. I, § 10; Ill. Const. art. I, § 16. Yet no one doubts that the police-powers limitation applies there. The Pension Clause is no different.

2. The Pension Clause's Use of the Words "Diminished or Impaired" Neither Compels Nor Allows Plaintiffs' Absolutist Interpretation.

Although Plaintiffs did not include the argument in their draft opinion that the circuit court adopted, they argued in their briefs below that the police-powers limitation does not apply because the Pension Clause both creates a "contractual relationship" and provides that the benefits of the relationship cannot be "diminished or impaired." C2235. Plaintiffs thus claimed that this language evidences a purpose that is separate from its purpose to create an enforceable contractual relationship. C2235. But this analysis is simply wrong and is

inconsistent with the plain meaning of the Clause.

First, Plaintiffs' argument depends upon a misreading of the Pension Clause. The Clause says that membership in a public pension system is a contractual relationship, "the benefits *of which* shall not be diminished or impaired." Ill. Const. art. XIII, § 5 (emphasis added). The latter phrase is part of a dependent clause that relates back to the "contractual relationship" the Pension Clause establishes. In other words, the benefits that may not be "diminished or impaired" are the benefits *of* the "contractual relationship" — a relationship that, as a matter of settled law, is inherently limited by the State's police powers. Just as clearly, the Clause does not say that the benefits of membership *themselves* shall not be diminished or impaired. Plaintiffs' effort to elide the distinction that the Clause makes is nothing less than a refusal to acknowledge its plain and unambiguous meaning.

Second, Plaintiffs below claimed that their reading is necessary to avoid surplusage. C2287. But under Plaintiffs' reading, the Clause's crucial mention of "enforceable contractual relationships" itself becomes surplusage. If the benefits of membership in a public pension system cannot be diminished or impaired in the absolute way Plaintiffs suggest, there is no need to describe them as part of an "enforceable contractual relationship." In fact, calling those benefits absolute is actually *inconsistent* with calling it an "enforceable contractual relationship" and indeed raises more questions than it answers. For example, a contractual relationship can be renegotiated. But if that renegotiation involved the reduction of future pension benefits, even if in exchange for valuable consideration, Plaintiffs would apparently treat the new arrangement as unconstitutional. After all, the new agreement would "diminish or impair" the

pension benefits. So for the Pension Clause to truly give effect to its promise of "enforceable contractual relationships," Plaintiffs' reading of it cannot stand.

Third, Plaintiffs below also separately claimed that the word "diminished" must be given a meaning that is distinct from the word "impaired," and that the word "diminished" must be understood to establish an absolute protection. C2236. Besides having the same surplusage problem as the prior argument, this argument also fails because, in fact, the phrase "diminished and impaired" does *not* refer to two different things, and as already explained, *supra* Part II.A.1., "impaired" in reference to contracts unquestionably allows for the exercise of police powers. For this reason, the court in *In re City of Detroit*, rejected a virtually indistinguishable claim. 504 B.R. 97 (Bankr. E.D. Mich. 2013). There, pension plans for the City of Detroit sought to avoid the bankruptcy court's power to modify obligations to system members by "asserting that under the Michigan Constitution, pension debt has greater protection than ordinary contract debt." *Id.* at 150. The plans linked their view to a distinction in the Michigan Constitution between a constitutional provision stating that "pension rights may not be 'impaired or diminished,'" and a provision stating that contractual rights were protected only from laws "impairing" them. *Id.* at 151. Rejecting that argument, the court held that the purpose and effect of the Michigan Constitution was to give the status of a "contractual right" to public pensions that, as in Illinois, *see infra*, were formerly treated as "gratuitous allowances that could be revoked at will." *Id.* at 151-53. As a result, the court held, there was, "linguistically, . . . no functional difference in meaning between 'impair' and 'impair or diminish.'" *Id.* at 152. The same reasoning applies here.

Indeed, the law, including cases from both this Court and the United States Supreme Court often uses "diminish" and "impair" interchangeably. For example, in *Allied Structural Steel Company*, the United States Supreme Court treated the terms as interchangeable by rejecting the view that the Contracts Clause, which prohibits *impairing* the obligations of contracts, "forbids only state laws that *diminish* the duties of a contractual obligor and not laws that increase them." 438 U.S. at 244 n.16 (emphasis added). As the Court explained an increase on one side of the contract would necessarily be a diminishment on the other, thus impairing the contract. *Id.* Similarly, a pre-1970 Illinois Supreme Court decision held that a law violated the constitutional protection against the impairment of contractual obligations because it "diminishe[d]" the obligor's performance. *Geweke v. Vill. of Niles*, 368 Ill. 463, 466 (1938). *See also Black's Law Dictionary* (9th ed., 2009) (defining "impair" as "to *diminish* the value of (property or property right)" and noting that "impair is commonly used in reference to *diminishing* the value of" contract rights) (emphasis added). Moreover, Illinois' provision was borrowed from New York, which had added a virtually identical Clause to its Constitution in 1938. And before 1938, the expression "diminish or impair" was used in New York law to convey a unitary meaning (like the expressions "cease and desist," "aid and abet," or "free and clear"), not two separate meanings. *See, e.g., Metro. Trust Co. v. Tonawanda Valley & C.R. Co.*, 8 N.E. 488, 489 (N.Y. 1886); *Eddy v. London Assur. Corp.*, 38 N.E. 307, 311 (N.Y. 1894). Thus, the Illinois Pension Clause neither requires nor allows the construction Plaintiffs advocate.

B. The History Surrounding the Adoption of the Pension Clause Refutes Plaintiffs' Claim that the Drafters Intended to Eliminate the State's Authority to Exercise Its Police Powers.

For the reasons already stated, there is no ambiguity in the plain meaning of the Pension Clause. But if there were any doubt about its meaning, the constitutional debates further demonstrate that pension benefits remain subject to the State's police powers. Of course, this Court has emphasized that courts "must be circumspect in attempting to draw conclusions based on what was said" about the Pension Clause during the floor debates of the 1970 Constitutional Convention. *Kanerva*, 2014 IL 115811, ¶ 44. But in this case, the Convention debates, when read in the context of the state of the law at the time, do not allow any inference that the Pension Clause was intended to cast aside the then-century-old, fundamental legal principle that all contracts can be modified pursuant to a legitimate exercise of a State's police powers.

Before the Pension Clause was added to the Illinois Constitution in 1970, participation in the vast majority of public pension plans was mandatory, not voluntary. As a result, this Court held that the expected benefits from those mandatory plans were not contractual rights, but "bounties" or "gratuities" that the General Assembly could change or even repeal at will. *Bergin v. Bd. of Trs. of the Teachers' Ret. Sys.*, 31 Ill. 2d 566, 574 (1964); *Jordan v. Metro. Sanitary Dist. of Greater Chi.*, 15 Ill. 2d 369, 382 (1958). Thus, only the members of the very few *voluntary* public pension plans had *contractual* rights to their pension benefits (protected by the Contracts Clauses of the United States and Illinois Constitutions) and could prevent the legislature from freely reducing their retirement benefits. *Bardens v. Bd. of Trs. of the Judges Ret. Sys.*, 22 Ill. 2d 56, 60 (1961); *People ex rel. Judges Ret. Sys. v. Wright*, 379 Ill. 328, 333 (1942).

Accordingly, as this Court has recognized, "[t]he primary purpose behind the inclusion of [the Pension Clause] was to eliminate the uncertainty surrounding public pension benefits created by the distinction between mandatory and optional pension plans." *McNamee*, 173 Ill. 2d at 440; *see also Buddell*, 118 Ill. 2d at 102 (stating that the Pension Clause "guarantees that all pension benefits will be determined under a contractual theory rather than being treated as 'bounties' or 'gratuities,' as some pensions were previously"); *Sklodowski*, 162 Ill. 2d at 147 (Freeman, J., concurring in part and dissenting in part); *see also Kraus v. Bd. of Trs. of Police Pension Fund*, 72 Ill. App. 3d 833, 848 & n.6 (1st Dist. 1979) (holding that "what the [Pension Clause] . . . has accomplished" is to extend the contractual line of cases "to all public employees, without regard to whether their participation in the pension system was mandatory or voluntary").

This purpose is explicit in the constitutional debates. Delegate Green, a sponsor of the provision, explained that "pension benefits under mandatory participation plans" were held to be "in the nature of bounties which could be changed or even recalled as a matter of complete legislative discretion," and that the Pension Clause was intended to make pension system memberships "enforceable contracts." 4 Record of Proceedings, Sixth Illinois Constitutional Convention ("Proceedings") at 2925. Delegate Lyons supported the provision by offering that he was "not shocked at the notion of vesting contractual rights in beneficiaries of pension funds." *Id.* at 2929. And Delegate Whalen reiterated that the Pension Clause "lock[ed] in the contractual line of cases into the constitution." *Id.*

The delegates thus focused explicitly on the distinction between gratuities, "which could be changed . . . as a matter of complete legislative discretion," *id.* at 2925 (comments of Delegate Green), and "contractual" rights, *id.* at 2929 (comments of Delegates Lyons and Whalen); *see also id.* at 2525 (comments of Delegate Green). But there was no expression of a desire by anyone at the Constitutional Convention to give pension benefits *greater* constitutional protection than the protection afforded to other contracts. And this history explains not only what the drafters intended, but it also shows that the Pension Clause is in no way superfluous to the Contracts Clause. Without the Pension Clause, most public pensions would receive no protection at all.

The debates surrounding a different constitutional provision confirm that the circuit court's decision conflicts with the delegates' shared understanding. The 1970 Constitution separately establishes that "[s]ubject only to the police power, the right of the individual citizen to keep and bear arms shall not be infringed." Ill. Const. art. I, § 22. Yet when asked whether the explicit mention of "the police power" in this provision implied that the State's police powers would not apply to any constitutional provision that did not mention it expressly, its sponsor, Delegate Foster, forcefully rejected the notion, responding: "Now, you can go through this whole constitution and say, 'What if we applied [police powers] to that section?' *It applies to every section, whether it is stated or not* . . . ." 3 Proceedings at 1689 (emphasis added). He further explained that in fact "the state's right to . . . provide for the public health, safety, welfare, and morals infringes on your right to free speech, infringes on your right of assembly, infringes on your right to be secure in your own home. . . ." *Id.*; *see also id.* at 1480-81 (Delegate Lawlor explaining that failure to mention limitations on right

of assembly from police powers expressly did not denote their non-existence); *cf. Bain Peanut Co. of Tex. v. Pinson*, 252 U.S. 499, 501 (1931) (Holmes, J.) ("The interpretation of constitutional principles must not be too literal. We must remember that the machinery of government would not work if it were not allowed a little play in its joints."). That representation, undisputed by any other delegate, establishes the delegates' understanding — well-established in precedent and principle — that the State's police powers apply to *every* provision of the Constitution.

That view is also supported by New York precedent construing the virtually identical provision in its constitution that served as the model for the Pension Clause. *See generally Buddell*, 118 Ill. 2d at 106-07 (relying on New York courts' interpretations of their constitutional provision to determine meaning of Pension Clause). Before that provision was added to the New York Constitution in 1938, that State's courts had held that public pensions established no contractual rights before a member retired and therefore could be modified or repealed by the legislature at will. *See Ayman v. Teachers' Ret. Bd.*, 172 N.E.2d 571, 573 (N.Y. 1961). Thus, the New York provision, just as in Illinois, was intended to confer previously unavailable "*contractual* protection upon the benefits of pension and retirement systems of the State" so that they were no longer "subject to the will of the Legislature" before a member's retirement. *Birnbaum v. New York State Teachers' Ret. Sys.*, 152 N.E.2d 241, 245 (N.Y. 1958) (emphasis added). It was not designed to confer the unheard-of protection of super-contractual status.

In fact, at the time of the 1970 Constitutional Convention, no court had ever recognized, or even contemplated, the possibility of a super-contractual

status for pension benefits that would exempt them entirely from the State's police power. Indeed, it appears that even today the only case in American legal history to do so is from a court interpreting a textually distinct pension provision that was adopted by another State twenty-eight years after the 1970 Illinois Constitutional Convention. *See Fields v. Elected Officials' Retirement Plan*, 320 P.3d 1160 (Ariz. 2014). The entire notion of super-contractual pension benefits was thus completely foreign to the delegates to the Illinois Constitutional Convention. And in the absence of constitutional language or any mention of abdicating police powers during the Convention debates, it strains credulity to suggest that the drafters were making such a radical change in law.

C. The Circuit Court and Plaintiffs Misconstrue This Court's Precedent Addressing the Pension Clause.

To the limited extent the circuit court purported to rely on this Court's precedent, it entirely misconstrued those cases. This Court's *only* decision addressing the application of the State's police powers to rights under the Pension Clause is *Felt*, 107 Ill. 2d 158. And in *Felt*, this Court considered a police-powers defense to a Pension Clause challenge on the merits. *Id.* at 166. *Felt* ultimately rejected the police-powers defense based on the evidence offered to support it in that particular case, but that does not change the fact that, contrary to the circuit court's holding, in*Felt*, this Court recognized that the State's police powers exist as a limitation on the contractual rights provided by the Pension Clause.

Felt addressed an amendment to the statutory formula used to calculate judicial pension benefits, which effectively decreased the pension of any judge who retired less than a year following a salary increase. 107 Ill. 2d at 160-61. This Court held that, for judges in service before the change, the amendment violated

both the Contracts Clause and the Pension Clause. *Id.* at 166-68. But *Felt* did not hold that the statutory change was *per se* invalid under the Pension Clause, much less declare that the plain meaning of the Pension Clause categorically exempted the contractual rights it established from any application of the State's police powers. Instead, it held that the *factual* basis offered to justify the change could not sustain the amendment as a proper exercise of the State's police powers. *Id.* at 166. This Court explicitly "recognized that 'the contract clause does not immunize contractual obligations from every conceivable kind of impairment or from the effect of a reasonable exercise by the States of their police power.'" *Id.* at 165-66 (quoting *George D. Hardin, Inc.*, 99 Ill. 2d at 103, and citing *Allied Structural Steel*, 438 U.S. at 241, *City of El Paso*, 379 U.S. at 509, and *Meegan v. Vill. of Tinley Park*, 52 Ill. 2d 354, 358 (1972)). It then observed that "presumably the defendants would offer a similar contention" based on the State's police powers "regarding [the Pension Clause] on the question of diminution and impairment of benefits." *Id.* at 166. But the Court did not reject that argument as *legally* irrelevant, as it would be under Plaintiffs' theory here. Instead, it reached the police-powers argument on the merits and found it insufficient on the *factual* record, stating:

> There is no indication *in the record before us*, however, that a significant number of judges, or the plaintiffs themselves, retired shortly after salary increases or that such retirements are a cause of the retirement system's underfunding.... The conclusion to be drawn is that the amendment severely impairs the retirement benefits of the plaintiffs and those similarly situated and *on the record here* is not defensible as a reasonable exercise of the State's police powers.

Id. at 166-67 (emphasis added).

The circuit court obscured *Felt*'s holding by taking other language from that opinion out of context in order to claim that *Felt* held that applying the State's police powers to rights protected by the Pension Clause would require it "'to ignore the plain language of the Constitution of Illinois.'" C2315 (A4) (quoting *Felt* 107 Ill. 2d at 167-68). But the circuit court relied on a part of the *Felt* opinion that came *after* the Court already had concluded that the State's police-powers argument was "not defensible as a reasonable exercise of the State's police powers" on the *factual* record. *Felt*, 107 Ill. 2d at 167. In fact, the language quoted by the circuit court constituted a separate response to the defendant's further claim that the Court should read the Pension Clause to conform to precedent from Alaska, Hawaii, and Michigan, whose constitutions each expressly prohibited reductions only in "accrued" pension benefits. *Id.* at 167. The circuit court thus erroneously relied on language this Court used only to explain that the pension modifications authorized by the specific qualification in those States' constitutions would be inconsistent with the Pension Clause. *Id.* at 167-68. In short, *Felt* not only provides no support for the circuit court's absolutist interpretation, it refutes that interpretation.

Nor does this Court's decision in *Kanerva,* which the circuit court cited, C2315 (A4), adopt the circuit court's super-contract reading of the Pension Clause. The only question presented in *Kanerva* was whether retiree health care subsidies are benefits within the *scope* of the protection provided by the Pension Clause. 2014 IL 115811, ¶¶ 1, 38. In holding that they are protected by the Clause, this Court had no occasion to consider the extent of that protection and, specifically, whether they are immune from the State's exercise of its police power, as Justice Burke noted in dissent. *Id.* at ¶¶ 91-93 (Burke, J., dissenting).

That fact is beyond dispute because of *Kanerva*'s procedural posture. When the *Kanerva* plaintiffs challenged reductions in the level of health care subsidies for retired system members, the defendants moved to dismiss the plaintiffs' claims on their face, arguing only that health care subsidies are not protected by the Pension Clause. Given the posture of that case, the defendants did not, and could not, invoke the State's police powers as a factual defense, as Defendants did here, meaning that this Court had no occasion to consider Plaintiffs' super-contract theory. *Kanerva* therefore cannot be deemed precedent on an issue it did not discuss or decide, and that it had no basis to decide. *See People v. Garcia*, 199 Ill. 2d 401, 408 (2002); *see Cates v. Cates*, 156 Ill. 2d 76, 81 (1993) (an opinion acts as precedent on specific issues before a court based on facts before it, and subsequent courts "must examine the authority cited by defendant within the context in which it arose").

In fact, *Kanerva* did not even cite *Felt*. Thus, the broad language in *Kanerva* that the scope of the Pension Clause does not "include restrictions and limitations that the drafters did not express and the citizens of Illinois did not approve," 2014 IL 115811, ¶ 41, and that doubts about the Clause's meaning should be resolved "in favor of the rights of the pensioner," *id.* at ¶ 55, must — like *Felt*'s language — be read in context. That context has to do with only what kinds of benefits fall within the Pension Clause. It has nothing to do with the question before the Court in this case.

Plaintiffs also attempted to argue below that this Court adopted their absolutist view of the Pension Clause in *Jorgensen v. Blagojevich*, 211 Ill. 2d 286 (2004). C1945-46, 2024. But *Jorgensen* did not even arise under the Pension Clause, as it involved judicial salaries (not pensions) and an application of the

Judicial Compensation Clause. Ill. Const. art VI, § 14 ("Judges shall receive salaries provided by law which shall not be diminished to take effect during their terms of office."). So while this Court held in *Jorgensen* that a statute eliminating previously approved cost-of-living increases for judicial salaries violated the Constitution, it did so based on a constitutional provision that is entirely different from the Pension Clause and on separation-of-powers principles that do not apply to contracts involving non-judicial public employees. 211 Ill. 2d at 305.

Furthermore, unlike the public employees at issue here, both *Jorgensen* and the case it principally relied upon, *People ex rel. Lyle v. City of Chicago*, 360 Ill. 25, 29 (1935), involved judges, who are not, in the constitutional sense, public "employees" with terms of service established and determined by an employment contract. *See Jorgensen*, 211 Ill. 2d at 303-05 (relying on *Lyle*). They are state "officers," with positions created by the Constitution, and they serve by election or appointment according to law. As a result, *Jorgensen* rightly never suggested that judicial salaries are based on a contractual right. *See People ex rel. Akin v. Loeffler*, 175 Ill. 585, 608 (1898) (following *Butler v. Pennsylvania*, 51 U.S. 402 (1850)); *Crumpler v. County of Logan*, 38 Ill. 2d 146, 150 (1967).

Lyle explains why that distinction is so critical. There, the Court specifically distinguished *contractual* rights, which it held are inherently subject to a State's police powers, from the constitutional provisions prohibiting reductions in judicial salaries during the judges' terms of office. *Lyle*, 360 Ill. at 29. In doing so, *Lyle* relied on the United States Supreme Court's opinion in *Home Building and Loan Association* to contrast the inherently qualified nature of the constitutional protection for *contractual* rights and the distinct constitutional protection for judicial salaries, which stand on an altogether

different footing. *Id.* at 29. In other words, *Jorgensen* relied upon authority that explicitly recognized that judicial salaries are unique for reasons of constitutional structure and separation of powers and that had nothing to do with the police-powers limitation on contracts.

The circuit court's extreme and unqualified interpretation of the Pension Clause thus cannot stand in the face of this Court's precedent. *Felt* applied the same police-powers test applicable to claims arising under the Contracts Clauses of the United States and Illinois Constitutions, and no other case purports even to address that question, much less overturn *Felt*. The Court should adhere to its prior precedent and reverse the decision of the court below.

III. The United States Constitution Does Not Permit a State to Abdicate Its Police Powers.

Not only does the circuit court's unbounded and unprecedented construction of the Pension Clause fly in the face of the Clause's plain meaning, but under the circuit court's construction, the Pension Clause violates the federal Constitution as applied to this case. That is because the Constitution forbids a State from "surrender[ing] an essential attribute of its sovereignty." *U.S. Trust Co.*, 431 U.S. at 23. And as the United States Supreme Court has long recognized, under this fundamental rule of federal constitutional law, sometimes called the "reserved powers doctrine," *see United States v. Winstar Corp.*, 518 U.S. 839, 888 (1996) (plurality), a state's police power is "an essential attribute of sovereignty" that cannot be abandoned. *U.S. Trust Co.*, 431 U.S. at 23.

It could hardly be otherwise. The very "maintenance of a government" requires that the State "retai[n] adequate authority to secure the peace and good order of society." *Home Bldg. & Loan Ass'n*, 290 U.S. at 434-35. Indeed, the

State has a duty to protect the public health, safety, and welfare of its citizens. *See Stone*, 101 U.S. at 819 ("No legislature can bargain away the public health or the public morals. . . . *Government is organized with a view to their preservation, and cannot divest itself of the power to provide for them.*") (emphasis added). The reserved powers doctrine thus constitutes "the application of the maxim, *salus populi suprema lex*," *Boston Beer Co.*, 97 U.S. at 33 (1877), meaning "the safety of the people is the supreme law," Black's Law Dictionary 1870 (9th ed. 2009); *see also Nw. Fertilizing Co. v. Hyde Park*, 70 Ill. 634, 644-45 (1873) ("To hold [that the State does not retain its police powers] is to reverse the rules of construction, the theory and policy of government, to change the principles on which it is based, to encroach upon the rights of the people, and to create a power in the State beyond its control and highly dangerous to the general welfare. Such immunity to these bodies was not intended by the framers of our government.").

Accordingly, the supremacy of the reserved powers doctrine has been emphasized repeatedly by the United States Supreme Court. In *Stone*, for example, the Supreme Court rejected a corporation's claim that a state charter to conduct lotteries immunized it from a state statute outlawing lotteries, enacted just one year after the charter. 101 U.S. at 817-18. In doing so, that Court declared not only that "the legislature cannot bargain away the police power of a State," but also that "*[t]he people themselves*" cannot "grant[] away" that power for future generations. *Id.* at 817, 819-20 (emphasis added).

The Court has never strayed from that bedrock constitutional principle. In *U.S. Trust Company*, the Court reiterated that a State is without "power to create irrevocable contract rights." 431 U.S. at 23 & n. 20. Or, as the Court stated in *Atlantic Coast Line R.R. v. City of Goldboro*, 232 U.S. 548, 558 (1914),

"the power of the State to establish all regulations that are reasonably necessary to secure the health, safety, good order, comfort, or general welfare of the community . . . can neither be abdicated nor bargained away, and is inalienable even by express grant." *See also Pierce Oil Corp. v. City of Hope*, 248 U.S. 498, 501 (1919) (observing that "a contract not to legislate if the public welfare should require it . . . would have no effect"). The reserved powers doctrine is thus "a principal of vital importance, and its habitual observance is essential to the wise and valid execution of the trust committed to the legislature." *Butchers' Union v. Crescent City*, 111 U.S. 746, 766 (1884) (Field, J., concurring).

Incredibly, the circuit court responded to the reserved powers doctrine by ignoring it. *See* C2312-17 (A1-6). Not one word of the court's opinion even mentions this first principle of our constitutional structure.[5] *Id.* That omission speaks volumes. The court conspicuously disregarded that the federal Constitution bars its holding that pensions are super-contracts uniquely exempt from the State's police powers. By ignoring this constitutional principle, the circuit court destroyed the carefully established balance between an individual's contractual rights and the government's duty to provide for the general welfare. At a minimum, these serious constitutional concerns trigger the constitutional avoidance canon, under which this Court must, if possible, construe the Pension Clause so as to avoid these profound constitutional questions. *See Villegas v. Bd. of Fire & Police Comm'rs*, 167 Ill. 2d 108, 124 (1995).

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[5] The same is true of two of the three briefs filed by Plaintiffs. *See* C2263, 2276. And the Plaintiffs that did acknowledge the doctrine were non-responsive. They argued that forcing the State "to pay pensions does not force the State to surrender its essential sovereign powers." C2243. That often may be true, but ignores the crux of the reserved powers doctrine: a State cannot commit that it will *never* apply its police powers *under any circumstance*.

That does not mean that the reserved powers doctrine renders agreements between government and private parties meaningless. As illustrated by the history of the Pension Clause, *see supra* Part III.B., and of state pensions before and after 1970, the Pension Clause created a strong protection that did not previously exist for members of public pension systems in Illinois. There is no question that under most circumstances, the reserved powers doctrine requires that a State's financial commitments are and should be enforced. *See U.S. Trust Co.*, 431 U.S. at 25 (noting that a "promise [that] is purely financial" is "not *necessarily* a compromise of the State's reserved powers" and will usually be enforced) (emphasis added). To depart from that norm and apply the police powers limitation, extraordinary circumstances must exist.

Here, however, the circuit court held that there is no set of facts that would ever justify any legislation negatively affecting pension benefits. That is untenable and unconstitutional. By construing the Pension Clause as sweeping away the State's police powers entirely, the circuit court construed the Pension Clause such that the Clause itself is unconstitutional. The federal Constitution requires that the State possess the flexibility to act in extreme circumstances. *U.S. Trust Co.*, 431 U.S. at 23; *Stone*, 101 U.S. at 817. Or, as the Supreme Court has emphasized, "while the Constitution protects against invasions of individual rights, it is not a suicide pact." *Kennedy v. Mendoza-Martinez*, 372 U.S. 144, 160 (1963); *see Terminiello v. City of Chi.*, 337 U.S. 1, 37 (1949) (Jackson, J., dissenting).

Furthermore, the Supreme Court has explained that the Constitution recognizes "two distinct limitations" that "protect state regulatory powers. One came to be known as the 'reserved powers' doctrine, which held that certain

substantive powers of sovereignty could not be contracted away." *Winstar Corp.*, 518 U.S. at 874; *see also id.* at 874 n.20 (identifying police powers as one of the substantive powers of sovereignty that cannot be surrendered). The second, often referred to as the "unmistakability doctrine," holds that, for those substantive powers of sovereignty that can be restricted, such as the taxing power, *see St. Louis v. United Rys. Co.*, 210 U.S. 266, 280 (1908), they "will [not] be held . . . to have been surrendered, unless such surrender has been expressed in terms too plain to be mistaken." *Winstar Corp.*, 518 U.S. at 874-75. Of course, the police power has been expressly held to be subject to the reserved powers doctrine, and thus not capable of surrender. *U.S. Trust Co.*, 431 U.S. at 23; *Butchers Union*, 111 U.S. at 752-53; *Stone*, 101 U.S. at 817. But even assuming *arguendo* that it were among the few sovereign rights that can be limited, the unmistakability doctrine still would preclude the circuit court's construction of the Pension Clause. *See United Rys. Co.*, 210 U.S. at 280 (holding that government's power to tax specific private entity unaffected by contract unless it "has been specifically surrendered in terms which admit of no other reasonable interpretation").

Under the unmistakability doctrine, a government's promise that purports to limit the exercise any of its sovereign powers can be construed to do so only when the claimed limitation is "clear and unmistakable," and even then will be "read narrowly and strictly." *N.Y. Rapid Transit Corp. v. City of N.Y.*, 303 U.S. 573, 590-91 (1938) (acknowledging state power to contractually grant tax exemptions). Yet despite this well-established doctrine, the circuit court concluded that the *absence* of an explicit reference to the State's police powers in the Pension Clause shows that the drafters of the Illinois Constitution intended to entirely eliminate them. *See* C2315 (A4). That has it backwards. The doctrine

requires that any such limitation — even in the unique circumstances where it is permissible — be explicit. The circuit court's construction of the Pension Clause thus violated this settled interpretive rule and should be reversed for that reason as well.

Accordingly, whether considered in light of either the reserved powers doctrine or the unmistakability doctrine, the circuit court's complete disregard of fundamental principles of federal constitutional law cannot stand.

IV. The Circuit Court Improperly Disregarded Section 97 of the Act, Which Makes Certain Provisions Inseverable and Others Severable.

Even if the Pension Clause precluded Defendants' police-powers defense, and it does not, the circuit court's judgment invalidating the entire Act would have to be reversed. The General Assembly enacted the Act to address a major fiscal and pension crisis in Illinois, and the reductions in the COLAs challenged by Plaintiffs account for the vast majority of the Act's savings. Nonetheless, the Act incorporates a variety of reforms to other aspects of state finance and operations. Specifically, the Act:

- changes the State's accounting method from the unit credit actuarial cost method to the entry age normal actuarial cost method, Pub. Act 98–599, §§ 5, 7 (amending 20 ILCS 3005/7, 8 and 30 ILCS 105/13, 24.15, 24.13);

- prohibits state-funded pension systems from using pension contributions to subsidize the costs of retiree health care programs, *id.* at § 15 (adding 40 ILCS 5/2–126.5, 14–133.5, 15–157.5, 16–152.5);

- prevents employees entering service after the Act's effective date from treating travel reimbursements as "compensation" when calculating a pension, *id.* (adding 40 ILCS 5/14–103.10(g));

- limits membership in SURS for employees who enter into service after the Act's effective date to employees of specific academic institutions, *id.* at § 15 (amending 40 ILCS 5/14–106, 14–107);

- amends definition of "teacher" entitled to TRS membership to exclude school board employees that enter into service after the Act's effective date, *id.* (amending 40 ILCS 5/16–106);

- prohibits collective bargaining over matters related to pension benefits, *id.* at §§ 3, 20 (amending 5 ILCS 315/4, 15 and 115 ILCS 5/4, 17; adding 5 ILCS 315/7.5 and 115 ILCS 5/10.5);

- prevents employees who enter into service after the Act's effective date from treating unused sick or vacation time as pensionable earnings, *id.* (amending 40 ILCS 5/7–114, 7–116, 9–219, 9–220, 14–104.3, 14–106, 15–112, 15–113.4, 16–121, 16–127, 17–116, 17–134); and

- prevents employees entering service after the Act's effective date from receiving a pension based upon their service to certain not-for-profit entities, *id.* (amending 40 ILCS 5/7–109).

The General Assembly distinguished these independent reforms from the Act's reforms related to state and employee contributions and COLA by placing only the latter within an "inseverability clause," which specifies that the provisions within its scope are "mutually dependent and inseverable from one another." *Id.* at § 97 (A18). The General Assembly then stipulated that the remaining reforms "are severable under Section 1.31 of the Statute on Statutes." *Id.*; *see* 5 ILCS 70/1.31 (2012).

Because, as explained *supra*, the COLA reforms are subject to the State's police-powers defense, it is unnecessary for the Court to resolve any question of severability at this time. But because the circuit court invalidated the Act as a whole, it cannot be overlooked that it erred in doing so, in addition to its error in rejecting the State's police powers defense. Thus this Court should reverse the

circuit court's holding that, despite the legislature's express intentions, no provision of the Act is severable from the provisions included in the inseverability clause. C2315-16 (A5).

This Court has been clear that it "presume[s] that the legislature intended to enact a statute that was consistent with our constitution" and thus "must give effect to as much of [a] statute as is possible." *People v. Warren*, 173 Ill. 2d 348, 371 (1996). Accordingly, when this Court invalidates a portion of a statute, it will invalidate the remainder of the law only if (1) "the valid and invalid portions of the statute are essentially and inseparably connected in substance" and (2) "the legislature would [not] have enacted the valid portions without the invalid portions." *People v. Alexander*, 204 Ill. 2d 472, 484 (2003) (internal quotations omitted). Neither criterion is met here.

Not even Plaintiffs have argued that the valid and purportedly invalid parts of the Act are "inseparably connected in substance." *Id.* Yet it is the settled law of this Court that "[i]f, when the unconstitutional portion is stricken out, that which remains is complete in itself and capable of being executed wholly independently of that which is rejected, it must be sustained." *McDougall v. Lueder*, 389 Ill. 141, 151 (1945). That is dispositive here. Reforms such as restrictions on changes to accounting methods and rules applying only to employees hired after the Act's effective date are "capable of being executed wholly independently" of state contribution and COLA reformd. In fact, Plaintiffs never asserted any constitutional challenge to most of the provisions outside Section 97, which for the most part do not impact the terms of any their contractual relationships with the pension systems.

And there is no basis for concluding that the General Assembly would have preferred no reforms to the reforms that all concede are constitutionally permissible. To the contrary, Section 97 differentiates between the reforms that were intended to stand if part of the legislation fell and those that were not. Although the presence of a severability provision is not alone dispositive, *see Best v. Taylor Mach. Works*, 179 Ill. 2d 367, 460-61 (1997) (observing that "an express severability clause may be viewed as a rebuttable presumption of legislative intent"), specific severability language is given significant deference, *People ex rel. Chicago Bar Ass'n v. State Bd. of Elections*, 136 Ill. 2d 513, 532-33 (1990).

It is no answer to this unmistakable declaration of legislative intent to argue that state contribution and COLA reforms are "important elements" of the General Assembly's response to the Illinois fiscal crisis. C2316 (A5). The fact that these "important elements" advance substantially the same basic objective as the other reforms does not render them inseverable. The opposite is true. With or without them, these additional reforms are consistent with the General Assembly's aim of stabilizing the State's finances. *See Best*, 179 Ill. 2d at 461-63. As a result, invalidation of some of the Act should not lead to complete frustration of the legislature's goals.

In the circuit court, Plaintiffs' severability argument amounted to an invitation for the court to immerse itself in the politics of the Act's passage and invalidate it entirely because, according to Plaintiffs, the Act would not have passed without the provisions listed in Section 97. C2250, 2300. Severability, however, is not an exercise in political handicapping. Rather, it is "essentially one of statutory construction." *Springfield Rare Coin Galleries, Inc. v. Johnson*, 115 Ill. 2d 221, 237 (1986). The task for the Court is not to divine the subjective

motivations of individual legislators, but to discern, using the tools of statutory construction, what the legislature intended should particular provisions be deemed unconstitutional. Plaintiffs below pointed to nothing in the Act showing that the General Assembly would have wanted to undo every one of the Act's myriad reforms — and forego the financial benefits those reforms provide — if only some sections were invalidated.[6] So while this Court should reverse the entirety of the circuit court's judgment, if it does not do so, it should, at a minimum, reverse the severability analysis.

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[6] Defendants do not dispute that some provisions outside the inseverability clause would fall if this Court affirms the circuit court's decision because the State's only defense of them relies on the State's police powers. *See* Pub. Act 98–599, § 15 (amending 40 ILCS 5/2–108, 2–108.1, 2–119, 2–119.1, 14–103.10, 14–107, 14–108, 14–110, 15–111, 15–135, 16–112, 16–121, 16–132, 16–133.2, 16–133, and adding 40 ILCS 5/2-105.1, 2-105.2, 14-103.40, 16-106.4).

But the circuit court also held that changes to the method for calculating the "effective rate of interest" for SURS members, which is outside Section 97, violated the Pension Clause, because "[i]t is uncontested that this change, too, would reduce pension annuity payments." C2314 (A3); *see* Pub. Act 98–599, § 15 (amending 40 ILCS 5/15–125, 15–136). That is untrue. Defendants argued below that even if "Public Act 98–599 is not a valid exercise of the State's police powers . . . this claim still would be without merit because [the Plaintiffs] cannot demonstrate any impairment of their contractual rights." C2189. The circuit court overlooked that this point does not relate to the State's police-powers defense.

CONCLUSION

For the foregoing reasons, the circuit court's judgment should be reversed and the matter remanded to the circuit court for further proceedings.

Dated: January 12, 2015

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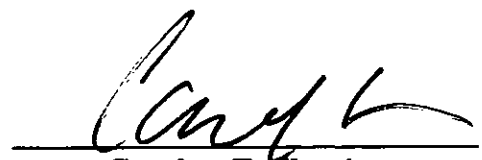
Rule 341(c) Certificate of Compliance

I certify that this Brief conforms to the form and length requirements of Supreme Court Rules 341(a) and (b). The length of this Brief, excluding the cover, the statement of points and authorities, this certificate of compliance, the certificate of filing and service by mail, and the separate appendix, is 50 pages.



Carolyn E. Shapiro

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IN THE CIRCUIT COURT FOR THE SEVENTH JUDICIAL CIRCUIT
SANGAMON COUNTY, ILLINOIS

IN RE: PENSION LITIGATION) No. 2014 MR 1
) Hon. John W. Belz
)

ORDER

This matter comes before the Court in these consolidated cases on the plaintiffs' joint motion for partial summary judgment, the *ISEA*, *RSEA*, *Heaton* and *Harrison* plaintiffs' joint motion for judgment on the pleadings as to the affirmative defense, or in the alternative, to strike the affirmative defense, and the *SUAA* plaintiffs' motion to strike the affirmative defense (the "Plaintiffs' Motions").

The plaintiffs in these consolidated cases allege that Public Act 98-0599 (the "Act") violates the Pension Protection Clause of the Illinois Constitution (Article XIII, §5) and that the Act is unconstitutional and void in its entirety. In their affirmative defense, the Defendants assert that the Act is justified as an exercise of the State's reserved sovereign powers or police powers. The Court hereby rules in favor of the plaintiffs on each motion and further finds and orders as follows:

1. The Pension Protection Clause of the Illinois Constitution states: "Membership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired." (Illinois Constitution, Article XIII, §5.) This constitutional language is "plain" and "unambiguous," and, therefore, the Pension Protection Clause is "given effect without resort to other aids for construction." *Kanerva v. Weems*, 2014 IL 115811, ¶¶ 36, 41-42. Under the Pension Protection Clause, "it is clear that if something qualifies as a benefit of the enforceable contractual relationship resulting from membership in one of the State's pension or retirement systems, it cannot be diminished or impaired." *Id.*, ¶ 38. The Illinois

legislature could not have been more clear that any attempt to diminish or impair pension rights is unconstitutional.

2. The Court finds that, on its face, the Act impairs and diminishes the benefits of membership in State retirement systems in multiple ways, including the following:

a. The Act adds new language to the Pension Code which provides that, on or after the Act's effective date, the 3% compounded automatic annual increases (AAIs) that have been mandated by the Pension Code for many years shall instead be "calculated as 3% of the lesser of (1) the total annuity payable at the time of the increase, including previous increases granted, or (2) $1,000 multiplied by the number of years of creditable service upon which the annuity is based . . . ." See the Act's amendments to 40 ILCS 5/2-119.1(a-1), 40 ILCS 5/15-136(d-1), 40 ILCS 5/16-133.1(a-1); see also the Act's amendments to 40 ILCS 5/14-114(a-1). The defendants admit that these amendments will reduce the AAI amounts that certain pension system members receive. See, *e.g.*, Answer to *Heaton* Amended Complaint, ¶¶ 43, 45, 47, 51, 55, 57, 61, 65; Answer to *Harrison* Complaint, ¶¶ 93-96, 133-140.

b. The Act also provides that State retirement system members who have not begun to receive a retirement annuity before July 1, 2014, will receive no AAI at all on alternating years for varying lengths of time, depending on their age. See the Act's amendments to 40 ILCS 5/2-119.1(a-2), 40 ILCS 5/14-114(a-2), 40 ILCS 5/15-136(d-2), 40 ILCS 5/16-133.1(a-2). The defendants admit that these amendments will reduce the AAI amounts that certain pension system members receive. See, *e.g.*, Answer to *Heaton* Amended Complaint, ¶¶ 13, 47, 51, 57, 61, 65; Answer to *Harrison* Complaint, ¶ 98; Answer to *SUAA* Amended Complaint, ¶¶ 142-45.

c. The defendants admit that Public Act 98-0599 also imposes a new cap on the

pensionable salary of members of certain State retirement systems. See, *e.g.*, the Act's amendments to 40 ILCS 5/16-121; see also, *e.g.*, Answer to *Harrison* Complaint, ¶¶ 100-04; Answer to *Heaton* Amended Complaint, ¶¶ 49, 67. That cap is the greater of: (1) the salary cap that previously applied only to members who joined the retirement system on or after January 1, 2011; (2) the member's annualized salary as of June 1, 2014; or (3) the member's annualized salary immediately preceding the expiration, renewal, or amendment of an employment contract or collective bargaining agreement in effect on June 1, 2014. See the Act's amendments to 40 ILCS 5/14-103.10(h), 40 ILCS 5/15-111(c), 40 ILCS 5/16-121; see also the Act's amendments to 40 ILCS 5/2-108. The new cap will reduce annuity payments, which are based in part on a pension system member's pensionable salary.

d. Public Act 98-0599 also raises the retirement age for members of certain State retirement systems on a sliding scale based upon one's age. See the Act's amendments to 40 ILCS 5/2-119(a-1), 40 ILCS 5/14-107(c), 40 ILCS 5/15-135(a-3), 40 ILCS 5/16-132; see also, *e.g.*, Answer to *Harrison* Complaint, ¶¶ 106-07; Answer to *Heaton* Amended Complaint, ¶¶ 48, 52, 58, 62, 66; Answer to *SUAA* Amended Complaint, ¶ 68.

e. The Act also alters "the method for determining the 'effective rate of interest' used to calculate pensions for members under the money-purchase formulas included in Articles 15 and 16 of the Pension Code." See Defendants' Affirmative Matter, ¶ 10; Answer to *SUAA* Amended Complaint, ¶¶ 64-67; see also the Act's amendments to 40 ILCS 5/15-125 and 40 ILCS 5/16-112. It is uncontested that this change, too, would reduce pension annuity payments.

3. The Act without question diminishes and impairs the benefits of membership in State retirement systems. Illinois Courts have consistently held over time that the Illinois Pension Clause's protection against the diminishment or impairment of pension benefits is absolute and

without exception. The Illinois Supreme Court has "consistently invalidated amendment to the Pension Code where the result is to diminish benefits." McNamee v. State, 173 Ill. 2d 433, 445 (1996). In their affirmative matter, the defendants assert that the Act is nonetheless justified as an exercise of the State's reserved sovereign powers or police powers. The Court finds as a matter of law that the defendants' affirmative matter provides no legally valid defense. The Court "may not rewrite the pension protection clause to include restrictions and limitations that the drafters did not express and the citizens of Illinois did not approve." *Kanerva*, 2014 IL 115811, ¶ 41. The Pension Protection Clause contains no exception, restriction or limitation for an exercise of the State's police powers or reserved sovereign powers. Illinois courts, therefore, have rejected the argument that the State retains an implied or reserved power to diminish or impair pension benefits. See *Felt v. Bd. of Trustees of Judges Retirement System*, 107 Ill.2d 158, 167-68 (1985) (holding that, to recognize such a power, "we would have to ignore the plain language of the Constitution of Illinois"); *Kraus v. Bd. of Trustees of Police Pension Fund of Vill. of Niles*, 72 Ill. App. 3d 833, 851 (1979).

4. Because the Act diminishes and impairs pension benefits and there is no legally cognizable affirmative defense, the Court must conclude that the Act violates the Pension Protection Clause of the Illinois Constitution. The Court holds that Public Act 98-0599 is unconstitutional.

5. The Act contains a "[s]everability and inseverability" clause. See Public Act 98-0599, §97. That provision states that the Act's changes to 39 distinct sections and subsections of various statutes "are mutually dependent and inseverable from one another," but that the Act is severable as a general proposition. *Id.* That list of 39 inseverable provisions includes certain of the benefit-reduction provisions that this Court has held to be unconstitutional. Therefore, all 39 provisions identified in the Act's "[s]everability and inseverability" clause must fail. Those

inseverable provisions are significant to the overall operation of the Act. They include, for example, the Act's mechanism for supposedly guaranteeing funding of the State pension systems. See Public Act 98-0599, §97. In addition, "severability" language is not dispositive. Notwithstanding the presence of a severability clause, legislation is not severable where, as here, it is a broad legislative package intended to impose sweeping changes in a subject area, and the unconstitutional provisions of that package are important elements of it. See *Cincinnati Ins. Co. v. Chapman*, 181 Ill.2d 65, 81-86 (1998); see also *Best* v. *Taylor Mach. Works*, 179 Ill.2d 367, 459-67 (1997). The Act's provisions "are all part of an integral bipartisan package." See 98th Ill. Gen. Assem., Senate Pro., Dec. 3, 2013, at 4 (Sen. Raoul). The Court holds that Public Act 98-0599 is inseverable and void in its entirety.

6. The defendants have attempted to create a factual record to the effect that, if a reserved sovereign power to diminish or impair pensions existed, the facts would justify an exercise of that power. The defendants can cite to no Illinois case that would allow this affirmative defense. Because the Court finds that no such power exists, it need not and does not reach the issue of whether the facts would justify the exercise of such a power if it existed, and the Court will not require the plaintiffs to respond to the defendants' evidentiary submissions. The plaintiffs having obtained complete relief, the Court also need not address at this time the plaintiffs' additional claims that the Act is unconstitutional or illegal on other grounds. *See Kanerva*, 2014 IL 115811, ¶ 58. In summary, the State of Illinois made a constitutionally protected promise to its employees concerning their pension benefits. Under established and uncontroverted Illinois law, the State of Illinois cannot break this promise.

WHEREFORE, the Court orders as follows:

a. The Plaintiffs' Motions are granted. The defendants' cross-motion for summary judgment is denied, with prejudice, because the Court finds that there is no police power or reserved

sovereign power to diminish pension benefits. Pursuant to 735 ILCS 5/2-701, the Court enters a final declaratory judgment that Public Act 98-0599 is unconstitutional and void in its entirety;

b. The temporary restraining order and preliminary injunction entered previously in this case is hereby made permanent. The defendants are permanently enjoined from enforcing or implementing any provision of Public Act 98-0599;

c. Pursuant to Illinois Supreme Court Rule 304(a), the Court finds that there is no just reason for delaying either enforcement of this order or appeal or both.

Date: 11/21/14

ENTERED:

Judge John W. Belz

IN THE CIRCUIT COURT FOR THE SEVENTH JUDICIAL CIRCUIT
SANGAMON COUNTY ILLINOIS

IN RE: PENSION LITIGATION	)	No. 2014 MR 1
	)	Honorable John W. Belz
	)	

Illinois Supreme Court Rule 18 Findings

On November 21, 2014, this Court entered an order granting plaintiffs' joint motion for partial summary judgment, granting plaintiffs' joint motion for judgment on the pleadings on defendants' affirmative defense and the SUAA plaintiffs' motion to strike defendants' affirmative defense, denying defendants' cross-motion for summary judgment, permanently restraining enforcement or implementation of the Act, and finding that no just reason to delay enforcement or appeal of the order existed. Because the November 21, 2014 order, which is incorporated herein by reference, invalidated a state statute, the Court enters these findings pursuant to Illinois Supreme Court Rule 18:

1. Public Act 98-0599 (the "Act") is unconstitutional in its entirety;

2. The Act violates the Pension Protection Clause of the Illinois Constitution, Ill. Const. art. XIII, § 5;

3. The Act is unconstitutional on its face;

4. The Act cannot be reasonably construed in a manner that would preserve its validity;

5. The finding of unconstitutionality of the Act is necessary to the judgment rendered and such judgment cannot rest upon an alternative ground; and

6. The notice required by Illinois Supreme Court Rule 19 has been served and those with such notice have been given adequate time and opportunity under the circumstances to defend the Act.

Date: 11/25/14 **Enter:** John W. Belz

IN THE CIRCUIT COURT FOR THE SEVENTH JUDICIAL CIRCUIT,
SANGAMON COUNTY, ILLINOIS

IN RE: PENSION REFORM LITIGATION	)	No. 2014 MR 1
	)	Hon. John W. Belz
This document relates to:	)	
	)	
DORIS HEATON, PAMELA KELLER, KENNETH LEE, HATTIE DOYLE, JOHN SAWYER III, Ed.D., LANCE LANDECK, KYLE THOMPSON, and MICHAEL SCHIFFMAN, on behalf of themselves and a class of similarly situated persons,	)	
Plaintiffs,	)	Originally Filed as
v.	)	Cook County Case No.
PAT QUINN, Governor of the State of Illinois, in his official capacity, JUDY BAAR TOPINKA, Comptroller of the State of Illinois, in her official capacity, and THE BOARD OF TRUSTEES OF THE TEACHERS' RETIREMENT SYSTEM OF THE STATE OF ILLINOIS,	)	2013 CH 28406
Defendants.	)	

ANSWER AND DEFENSES

Defendants Patrick Quinn, in his official capacity as Governor of the State of Illinois, Judy Baar Topinka, in her official capacity as the Comptroller of the State of Illinois, and the Board of Trustees of the Teachers' Retirement System of the State of Illinois (collectively "Defendants") for their answer to the Amended Complaint filed by Plaintiffs Doris Heaton, *et al.*, state as follows:

1. The Constitution of the State of Illinois contains a guarantee relied upon by many thousands of active and retired teachers and school administrators for more than four decades. That guarantee, perhaps more so than anything else in the Illinois Constitution, was used by countless families across Illinois to plan careers, retirements and financial futures. When teachers and school administrators decided to continue educating Illinois children instead of transitioning to careers in the private sector or working elsewhere, when they decided where to send their children to college, and when they decided when and how to retire, they relied upon that guarantee. Many of them can recite that constitutional guarantee by heart. Its words are

will be irreparably harmed by the implementation and enforcement of Public Act 98-0599, have no adequate remedy at law, and are likely to succeed on the merits of this case. Any weighing of the equities would mandate the issuance of preliminary and permanent injunctive relief in favor of the plaintiffs and members of the class they represent.

ANSWER: Paragraph 70 contains legal conclusions that Defendants deny. To the extent Paragraph 70 contains any factual allegations, Defendants deny those allegations.

AFFIRMATIVE MATTER IN DEFENSE OF CLAIMS ASSERTED
(Reserved Sovereign Powers)

Pursuant to Section 2-613(d) of the Code of Civil Procedure, Defendants further respond to the Amended Complaint by alleging the following affirmative matter in defense of the claims asserted by the plaintiffs in this suit:

1. All causes of action asserted in the Plaintiffs' Complaint fail to state a claim and are barred because Public Act 98-599 (the "Act") is a permissible exercise of the State of Illinois' reserved sovereign powers (sometimes referred to as the State's police powers). Plaintiffs cannot sustain their burden of establishing that Public Act 98-599 is unconstitutional.

2. Starting around 2000 and continuing through the financial crisis and deep recession that began in 2008, underfunding in the state-funded retirement systems (*i.e.*, asset levels below the actuarially required amounts needed to pay all benefits for services provided by members) contributed significantly to a severe financial crisis for the State that adversely affected the long-term financial soundness of those retirement systems, the cost of financing the State's operations and outstanding debt, and the State's ability to provide critical services to Illinois residents and businesses.

3. From fiscal year 1999 to fiscal year 2013, the unfunded actuarial liability of the four state-funded retirement system affected by Public Act 98-599 (hereinafter the "Systems"),

according to the Systems' actuarial reports for those years, increased as follows (rounded to the nearest million dollars):

	1999	2013
TRS	$10,968,000,000	$55,732,000,000
SERS	$2,012,000,000	$22,843,000,000
SURS	$1,855,000,000	$20,110,000,000
GARS	$94,000,000	$269,000,000
Total:	$14,929,000,000	$98,954,000,000

The causes of this underfunding included, but were not limited to, significant unforeseen and unanticipated events, including, among other things: (1) prolonged and unusually poor investment results and reasonable future investment return expectations due to systemic, severe market downturns, including in the wake of the worst financial crisis since the Great Depression; (2) historically low rates of inflation; (3) significant increases in life expectancy; and (4) other changes in actuarial assumptions. These events not only increased significantly the Systems' unfunded actuarial liabilities, but also led to substantial reductions in the State's revenues available to make contributions to the Systems and for other expenditures, including wages, salaries and other benefits for state employees.

4. Although the Systems have been underfunded for many years, their underfunding now greatly exceeds the State's annual budget for all categories of expenditure, including, without limitation, public education, public health and safety, medical coverage for the poor and for current and retired public employees, road construction, repair and maintenance, and all other public services provided by state employees.

5. Before passage of the Act, the Systems' unsustainable and worsening liabilities greatly contributed to higher debt financing costs for the State, which passage of the Act immediately and substantially alleviated. The Systems' unsustainable and worsening pension liabilities, which the Act was intended to address, also contributed to substantial uncertainty in the State's climate for attracting and retaining businesses that provide employment to Illinois residents, contribute to a thriving state economy, and pay taxes that support important public services and provide revenues to fund the Systems. A significant factor contributing to the magnitude of System's liabilities and corresponding underfunding is that the 3% compounded annual annuity increases, which are not part of the core pension benefit, have in recent years substantially exceeded actual inflation and were not matched with higher employee contributions.

6. Before enacting Public Act 98-599, the General Assembly took multiple other steps to address the State's financial crisis, including the increasingly urgent problem presented by the Systems' underfunding. Those steps included, among other things, enacting a separate program of less generous pension benefits for persons who became system members after 2010 (identified as "Tier II" members); significantly reducing public spending on other programs, including support for public education, Medicaid, health insurance benefits for current and retired state employees, and other social services for Illinois residents; raising income taxes; and deferring billions of dollars in payments owed to state vendors and other creditors. These measures proved insufficient to adequately address the State's financial crisis, and its credit rating continued to suffer, causing it to incur still higher costs to finance its debt, thereby further reducing the revenues that could be devoted to providing critical services to Illinois residents and reducing the Systems' unfunded liabilities.

7. Only after taking these other measures to promote the actuarial soundness of the Systems and address the State's financial crisis resulting from this underfunding problem did the General Assembly pass the Act, which includes a schedule for actuarially prescribed, automatic state contributions to the Systems that will progressively eliminate their underfunding, a mechanism for enforcing those contributions, reductions in contributions to the Systems by their active members, and for persons who became members of the Systems before 2011 (referred to as "Tier I" members), modifications to future pension increases for active and retired members.

8. The pension modifications provided in the Act include prospective reductions in future increases in annual annuity adjustments (often referred to as cost-of-living adjustments, or COLAs) that are designed to have the least impact on members with the lowest salaries on which their pensions are calculated, on members who put in the most years of public service, and on members who retired before July 1, 2014.

9. The pension modifications provided in the Act also include increases in the retirement age at which active members below the age of 46 are entitled to receive a pension. Those increases, up to a maximum of five years, are lowest for the oldest active members and are progressively greater for younger active members.

10. The pension modifications provided in the Act further include a cap on the pensionable salary of active members with a salary presently above about $110,000, and a change in the method for determining the "effective rate of interest" used to calculate pensions for members under the money-purchase formulas included in Articles 15 and 16 of the Pension Code.

11. In light of the above-described unanticipated exigencies contributing to the Systems' unsound financial condition and the State's related fiscal crisis, the Act represented a

reasonable response to these circumstances. In light of the measures already taken by the General Assembly to address the Systems' financial condition and the State's fiscal crisis, and in light of the serious negative effects of other alternatives, the Act's limited changes to pensions were necessary to address these circumstances.

12. The legislative findings in the Act include the following:

a. "Illinois has both atypically large debts and structural budgetary imbalances that will, unless addressed by the General Assembly, lead to even greater and rapidly growing debts and deficits. Already, Illinois has the lowest credit rating of any state, and it faces the prospect of future credit downgrades that will further increase the high cost of borrowing."

b. "The State has taken significant action to address these fiscal troubles, including, but not limited to, increasing the income tax and reducing pension benefits for future employees. Further, the State has enacted a series of budgets over the last several fiscal years that resulted in deep cuts to important discretionary programs that are essential to the people of Illinois."

c. "[T]he State's retirement systems have unfunded actuarially accrued liabilities of approximately $100 billion."

d. "[W]ithout significant pension reform, the unfunded liability and the State's pension contribution will continue to grow, and further burden the fiscal stability of both the State and its retirement systems."

e. "Having considered other alternatives that would not involve changes to the retirement systems, the General Assembly has determined that the fiscal problems facing the State and its retirement systems cannot be solved without making some changes to the structure of the retirement systems. As a result, this amendatory Act requires more fiscal responsibility of the State, while minimizing the impact on current and retired State employees."

13. These legislative findings are reasonable and justified. They confirm and establish that the Act represents a reasonable and necessary means by the General Assembly to achieve an important public purpose.

14. The Act is presumed constitutional. The Act's presumption of constitutionality includes the reasonableness and necessity for its provisions in light of the circumstances faced by the State and the General Assembly when it was enacted.

15. In light of the magnitude of the pension problem and all of the other efforts the State has made to date, the Act represents a valid exercise of the State's reserved sovereign powers to modify contractual rights and obligations, including contractual obligations of the State established under Article I, Section 16 and Article XII, Section 5 of the Illinois Constitution.

WHEREFORE, Defendants pray for entry of judgment in their favor and against the plaintiffs on all of their claims, and for such further relief as is warranted in the circumstances.

Date: May 15, 2014

Respectfully Submitted,

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CONSTITUTIONAL PROVISION INVOLVED

ARTICLE XIII—GENERAL PROVISIONS

Section 5. Pension and Retirement Rights.

> Membership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.

STATUTORY PROVISIONS INVOLVED

PUBLIC ACT 098-599—SB0001 Enrolled

AN ACT concerning public employee benefits.

Be it enacted by the People of the State of Illinois, represented in the General Assembly:

Section 1. Legislative statement.

At the time of passage of this amendatory Act of the 98th General Assembly, Illinois has both atypically large debts and structural budgetary imbalances that will, unless addressed by the General Assembly, lead to even greater and rapidly growing debts and deficits. Already, Illinois has the lowest credit rating of any state, and it faces the prospect of future credit downgrades that will further increase the high cost of borrowing.

The State has taken significant action to address these fiscal troubles, including, but not limited to, increasing the income tax and reducing pension benefits for future employees. Further, the State has enacted a series of budgets over the last several fiscal years that resulted in deep cuts to important discretionary programs that are essential to the people of Illinois.

At the time of passage of this amendatory Act of the 98th General Assembly, the State's retirement systems have unfunded actuarially accrued liabilities of approximately $100 billion. Mean-

while, the State's annual pension contribution has substantially increased in recent years, and will continue to increase in coming years. The General Assembly recognizes that without significant pension reform, the unfunded liability and the State's pension contribution will continue to grow, and further burden the fiscal stability of both the State and its retirement systems.

This amendatory Act of the 98th General Assembly is intended to address the fiscal issues facing the State and its retirement systems in a manner that is feasible, consistent with the Illinois Constitution, and advantageous to both the taxpayers and employees impacted by these changes. Having considered other alternatives that would not involve changes to the retirement systems, the General Assembly has determined that the fiscal problems facing the State and its retirement systems cannot be solved without making some changes to the structure of the retirement systems. As a result, this amendatory Act requires more fiscal responsibility of the State, while minimizing the impact on current and retirement State employees.

Going forward, the automatic annual increase in retirement annuity will be based on a participant's years of service to the State and inflation, which more accurately reflects changes in the cost of living. For participants who have yet to receive an annuity, a pensionable salary cap will be imposed; however, it will only impact future salary increases that exceed a cap. Those workers 45 years of age and younger will be required to work an additional 4 months for each year under 46, which results in a minimal increase in retirement age given that life expectancy for a 45 year old is 87 years of age. Current employees will receive a 1% reduction in required employee contributions. With these changes, the State can adopt an actuarially sound funding formula that will result in the pension systems achieving 100% funding no later than 2044. The State will also make additional contributions that will considerably aid in reducing the unfunded actuarially accrued liability.

The General Assembly finds that this amendatory Act of the 98th General Assembly will lead to fiscal stability for the State and its pension systems.

Section 97. Severability and inseverability.

The provisions of this Act are severable under Section 1.31 of the Statute on Statutes, except that the changes made to Sections 20 and 25 of the Budget Stabilization Act and to subsections (a), (a-1), (a-2), (b), and (d) of Section 2-119.1, subsections (d), (d-1), and (d-2) of Section 15-136, subsection (a-10) of Section 16-158, and Sections 2-124, 2-125, 2-126, 2-134, 2-165, 14-114, 14-115, 14-131, 14-132, 14-133, 14-135.08, 14-155, 15-155, 15-156, 15-157, 15-165, 15-200, 16-133.1, 16-136.1, 16-152, 16-158, 16-158.2, 16-205, 20-106, 20-121, 20-123, 20-124, and 20-125 of the Illinois Pension Code are mutually dependent and inseverable from one another but are severable from any other provision of this Act.

APPEAL TO THE
SUPREME COURT OF ILLINOIS

From the Circuit Court for the Seventh Judicial Circuit,
Sangamon County, Illinois

IN RE: PENSION REFORM LITIGATION	)	No. 2014 MR 1 Hon. John W. Belz
DORIS HEATON, *et al.*, Plaintiffs-Appellees, v. PAT QUINN, Governor of Illinois, *et al.*, Defendants-Appellants.	)	Originally Filed as Cook County Case No. 2013 CH 28406
RETIRED STATE EMPLOYEES ASS'N RETIREES, *et al.*, Plaintiffs-Appellees, v. PATRICK QUINN, Governor of Illinois, *et al.*, Defendants-Appellants.	)	Originally Filed as Sangamon County Case No. 2014 MR 1
ILLINOIS STATE EMPLOYEES ASS'N, *et al.*, Plaintiffs-Appellees, v. BOARD OF TRUSTEES OF STATE EMPLOYEES RETIREMENT SYSTEM OF ILLINOIS, *et al.*, Defendants-Appellants.	)	Originally Filed as Sangamon County Case No. 2014 CH 3
GWENDOLYN A. HARRISON, *et al.*, Plaintiffs-Appellees, v. PATRICK QUINN, Governor of Illinois, *et al.*, Defendants-Appellants.	)	Originally Filed as Sangamon County Case No. 2014 CH 48
STATE UNIVERSITIES ANNUITANTS ASS'N, *et al.*, Plaintiffs-Appellees, v. STATE UNIVERSITIES RETIREMENT SYSTEM, *et al.*, Defendants-Appellants.	)	Originally Filed as Champaign County Case No. 2014 MR 207

Notice of Appeal

A19

Defendants, Illinois Governor Pat Quinn, *et al.*, by their counsel, Illinois Attorney General Lisa Madigan, (1) appeal to the Supreme Court, pursuant to Supreme Court Rule 302(a), from the circuit court's November 21, 2014 order, as supplemented by the circuit court's November 25, 2014 findings pursuant to Supreme Court Rule 18 (copies of which are attached as Exhibits A and B) (collectively, the "Judgment"), which, among other things, (a) entered judgment in favor of all of the plaintiffs in these consolidated cases on their claims that various provisions of Public Act 98–599 (the "Act") violate the Pension Clause of the Illinois Constitution (art. XIII, § 5), (b) declared the Act void in its entirety, and (c) entered a finding pursuant to Supreme Court Rule 304(a) that there is no just reason to delay enforcement or appeal; and (2) request (a) reversal of the Judgment, (b) remand for the purposes of addressing the merits of all of the plaintiffs' claims, including the merits of the plaintiffs' Pension Clause claims in light of the affirmative matter alleged in the defendants' answers, and (c) such further relief as is warranted.

Respectfully submitted,

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